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Memorandum

R-129-3113

To: The Honorable Mike Foley
Ohio House of Representatives

From: Todd Celmar, Economist TC

Date: February 14, 2012

Subject: Impact of federal sequestration on Ohio

This memorandum responds to your request for an analysis on the impact to Ohio of the automatic reductions to federal grants, referred to as "sequestration," expected to occur due to the Congressional Joint Select Committee on Deficit Reduction not agreeing upon deficit reduction measures by the established deadlines. Due to sequestration, in federal fiscal year (FFY) 2013, Ohio may experience a loss of federal revenue of about \$312.6 million, which represents a 1.3% loss of federal revenue from the FFY 2012 level of \$23.95 billion. The loss of federal revenue would continue through FFY 2021, though at slightly less amounts each year. The decrease would mainly affect state agencies as well as universities, local governments, and municipal housing authorities.

Spreadsheets

The enclosed spreadsheets list the federal grants received by Ohio that would be subject to sequestration. The spreadsheets include the grant amounts for FFY 2011, estimated grant amounts for FFY 2012 (based on federal legislation), and the estimated reduction in federal funds in FFY 2013 due to sequestration. Grants are grouped by the overseeing federal agency and listed from the largest reduction to smallest within each general function category. As shown in the spreadsheets, the largest reductions (in terms of dollar amount) are to grants administered by the federal departments of Education and Health and Human Services. Information in the spreadsheets was provided by the nonprofit and nonpartisan organization Federal Funds Information for States (FFIS).

Assumptions

FFIS estimated that grants subject to sequestration would decrease by 8.8% from FFY 2012 to FFY 2013. This estimate is based on a number of assumptions on how sequestration will occur in accordance with the Budget Control Act (BCA) and with other federal laws governing the process. First, it is assumed that the \$1.2 trillion in total federal spending reductions required by the BCA will result in \$984 billion in actual cuts with the remaining \$216 billion saved from reduced interest payments. When spread over nine years (FFY 2013-FFY 2021), reductions would equal about \$109 billion each year. As the BCA splits reductions 50/50 between defense and nondefense programs, nondefense reductions would amount to about \$54 billion each year. Of the reductions to nondefense spending, mandatory programs such as Medicare are subject to a 2% reduction, which in FFY 2013 is estimated to total about \$10 billion.¹ Therefore, the estimate of cuts to nondefense discretionary programs is \$44 billion. Of this amount, it is estimated that about \$9.2 billion would need to come from discretionary federal grants to states and local government entities. A \$9.2 billion reduction amounts to an "across the board" cut of about 8.8% for most grants in FFY 2013 from the FFY 2012 funding levels.

FFIS cautions that the estimates are "hypothetical" and are designed to help states understand the *potential* for reductions, as it is not possible to know the exact implications of the federal sequestration process on federal grants.² The actual percentage reductions will be determined by the federal Office of Management and Budget using enacted FFY 2013 appropriations and baseline projections pertaining to interest rates and other factors made at that time.

Exemptions

The majority of federal funding to states is exempt from sequestration. Though most *funding* is exempt, most of the federal grants to states – 156 out of the 210 grants tracked by FFIS – are not exempt. These grants account for about 18% of total federal funding to states. For instance, based on data from FFIS, of the estimated \$23.95 billion in federal grants for Ohio in FFY 2012, federal grants exempted from sequestration account for \$20.35 billion (85.0%), while grants that are subject to sequestration account for \$3.60 billion (15.0%). Major exempted grants include federal reimbursement received for Medicaid, the Temporary Assistance for Needy Families Block Grant, the Supplemental Nutrition Assistance Program (formerly referred to as Food Stamps), and certain child nutrition programs. These programs as well as most of the other exempted

¹ Medicare reductions would apply to payments to providers, not to benefits.

² Other organizations estimate reductions generally ranging from 7.5% to 9.5%. FFIS used the 8.8% estimated based on estimates used by the National Governor's Association.

programs are "mandatory" programs.³ Most of the programs subject to sequestration are "discretionary" programs.

Discretionary and mandatory programs

Discretionary and mandatory programs are funded differently by Congress, and therefore will be affected differently by the sequestration process. For discretionary programs, Congress sets the levels of expenditures each year for each program. In FFY 2013, sequestration would apply to all discretionary programs equally, as shown in the spreadsheets. Then, beginning in FFY 2014, sequestration would apply only toward *total* expenditures; Congress could reduce expenditures for some grants by larger percentages than others as long as the total amount remains under the reduced expenditure cap. Mandatory programs, which include Medicare, are funded by Congress based on eligibility and payment criteria established for each program. For these programs, sequestration would take place automatically each year for each program. Mandatory programs will be reduced by 2% each year. Because Medicare is forecasted to grow over the next ten years, the 2% reduction to Medicare will be a larger dollar amount each year, and will account for a larger share of total reductions. Therefore, discretionary grants listed in the spreadsheets will likely be reduced by gradually smaller percentages each year. The Congressional Budget Office estimates that discretionary grants will be reduced by 8.7% in FFY 2014, and by about 7.1% in FFY 2021.

If you have any questions, please contact me at (614) 466-7358 or tcelmar@lsc.state.oh.us.

Enclosure: Federal Grants to Ohio Subject to Sequestration

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³ In the spreadsheets the few mandatory programs that are subject to sequestration are designated with "(Mandatory)" after the name of the grant.