COLORADO GENERAL ASSEMBLY
JOINT BUDGET COMMITTEE

FY 2008-09 SUPPLEMENTAL

TOBACCO-SETTLEMENT FUNDED PROGRAMS

JBC Working Document - Subject to Change
Staff Recommendation Does Not Represent Committee Decision

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Supplemental Adjustments Required by Current Law

JBC Staff-Initiated Supplemental
Adjustments to the appropriations for tobacco-settlement-supported programs, funds, projects, and agencies.

FY 2008-09 allocations and appropriations of settlement revenues to:	Allocation Forecast at Time FY 2008-09 Long Bill Appropriations were set*	Actual FY 2008-09 Allocation*	Actual Allocation vs Forecast	Related Appropriation (CF) in FY 2008-09 Long Bill†	Recommended Change to FY 2008-09 Appropriation
Total Allocation to Tier 1 and Tier 2 Programs	**$106,653,987**	**$103,640,387**	**($3,452,088)**		
Tier 1 Programs - Total allocation	**67,993,343**	**66,811,204**	**(1,620,627)**		
Nurse Home Visitor Program	13,845,461	13,453,722	(391,739)	13,845,461	(391,739)
Fitzsimons Lease Purchase (Appropriation completely specified by statute)††	8,000,000	8,000,000	0	8,000,000	0
Read-to-achieve grant program	5,325,177	5,174,508	(150,669)	6,675,177	(150,669)
Tony Grampsas Youth Services Program (Appropriation completely specified by statute)	4,260,142	4,139,607	(120,535)	4,260,142	(120,535)
Ryan White HIV/AIDS Drug Assistance Program (Appropriation completely specified by statute)	3,727,624	3,622,156	(105,468)	3,727,624	(105,468)
HIV and AIDS Prevention Grant Program	1,997,179	1,997,101	(78)	3,139,141	0
State Veterans Trust Fund Expenditures	998,589	998,551	(38)	627,500	0

PROGRAMS FUNDED WITH TOBACCO SETTLEMENT PAYMENTS
FY 2008-09 SUPPLEMENTAL RECOMMENDATION
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FY 2008-09 allocations and appropriations of settlement revenues to:	Allocation Forecast at Time FY 2008-09 Long Bill Appropriations were set*	Actual FY 2008-09 Allocation*	Actual Allocation vs Forecast	Related Appropriation (CF) in FY 2008-09 Long Bill†	Recommended Change to FY 2008-09 Appropriation
Dental Loan Repayment Program	200,000	200,000	0	246,131	0
Child Mental Health Treatment Act (Appropriation completely specified by statute)	300,000	300,000	0	300,000	0
Children with Autism (Appropriation determined by program needs)	500,000	900,000	400,000	273,607	Melodie will make recommendations
State Auditor (Appropriation completely specified by statute)	83,214	83,214	0	83,214	0
Tier 1 allocation to Children's Basic Health Plan (There are more appropriations to this program in Tier 2)	25,560,851	24,837,640	(723,211)		Melodie will make recommendations
Tier 1 allocation to Comprehensive Primary and Preventive Care Grant Program. (There are more appropriations to this program in Tier 2)	3,195,106	3,104,705	(90,401)	6,481,973	Melodie will make recommendations
Tier 2 (S.B. 07-97) Programs - Total allocation	**38,660,644**	**36,829,183**	**ERROR!**		
Tier 2 allocation to Children's Basic Health Plan (There are more appropriations to this program in Tier 1) (Appropriation completely specified by statute)	1,933,032	1,841,459	(91,573)		Melodie will make recommendations
Tier 2 allocation to Comprehensive Primary and Preventive Care Grants (There are more appropriations to this program in Tier 1) (Appropriation completely specified by statute)	3,286,155	3,130,481	(155,674)	6,481,973	Melodie will make recommendations

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FY 2008-09 allocations and appropriations of settlement revenues to:	Allocation Forecast at Time FY 2008-09 Long Bill Appropriations were set*	Actual FY 2008-09 Allocation*	Actual Allocation vs Forecast	Related Appropriation (CF) in FY 2008-09 Long Bill†	Recommended Change to FY 2008-09 Appropriation
University of Colorado Health Sciences Center (Appropriation completely specified by statute)	18,943,716	18,046,300	(897,416)	18,943,716	(897,416)
Offender Mental Health Services‡ (Appropriation completely specified by statute)	4,639,277	4,419,502	(219,775)	4,173,152	246,350 Caroline will make further recommendations
Grants to Local Public Health Services (Appropriation completely specified by statute)	2,706,245	2,578,043	(128,202)	2,706,245	(128,202)
Supplemental State Contribution for Group Benefit Plans (Continuously appropriated).	1,739,729	1,657,313	(82,416)	0	0
Colorado Immunization Program** (Appropriation completely specified by statute). A portion of the appropriation is to CDPHE and a portion is to HCPF. Staff recommends that the CDPHE appropriation be decreased.	1,546,426	1,473,167	(73,259)	1,546,426	(73,259)
Alcohol and Drug Abuse Programs‡ (Appropriation completely specified by statute)	1,159,819	1,104,875	(54,944)	1,043,689	61,186 Caroline will make further recommendations
Medicaid Shortfalls at the Pediatric Trauma Center (Appropriation completely specified by statute)	386,606	368,292	(18,314)	386,606	(18,314)
Short Term Innovative Health Grants Program	2,319,639	2,209,751	(109,888)	2,959,390	0

For completeness staff has included all settlement supported programs in the above table, including those for which no change in the appropriation is recommended.

* By the time tobacco figure setting occurred during the 2008 session, the Department of Health Care Policy and Financing (HCPF) had submitted the first of four FY 2008-09 funding-need estimates for the Children with Autism program. Knowing that the first estimate would be revised shortly after tobacco figure setting, JBC staff used this estimate to forecast that the autism program would require an allocation of $500,000 of tobacco-settlement money and then used this forecast to compute the Tier 2 allocations for figure setting. After tobacco figure setting concluded, staff received HCPF's second FY 2008-09 autism-need forecast, which allowed staff to project that the autism program would require an allocation of $273,607 for FY 2008-09. The Committee approved this allocation for autism during 2008 HCPF figure setting. Though this change to the FY 2008-09 autism allocation meant the forecast of allocations to Tier 2 programs for FY 2008-09 had changed, Staff did not return to the Committee during the 2008 session to recommend modifications to the Tier 2 appropriations; knowing that further HCPF autism funding-need forecasts would later become available, staff chose to wait for January 2009 supplementals to present further recommended changes. At the current time, staff is aware that autism program expenditures have surged but will not receive HCPF's final forecast of FY 2008-09 autism program need for several weeks, which is too late for these supplementals. Thus the $900,000 "actual allocation" for autism for FY 2008-09 presented in this table is actually a revised forecast, one that is based on the most recent HCPF data. In summary, uncertainty about the needs of the Children with Autism program, which will not be resolved until mid-February 2009, makes it impossible to set the appropriations for Tier 2 programs exactly as prescribed by statute.

† The appropriation to the State Auditor appears in the legislative appropriations bill (H.B. 08-1361). In the cases where the Long Bill appropriation exceeds the allocation, the program is spending from its cash fund.

†† The notation "Appropriation completely specified by statute" means that statutory formulas specifies the exact amount of the appropriation, though in several cases this total is divided among two or more Long Bill lines and the division is not controlled by statute.

‡ The Long Bill appropriations for Offender Mental Health Services should have totaled $4,639,277; however, due to a technical error, the appropriations actually totaled $4,173,152. The appropriations for Alcohol and Drug Abuse should have totaled $1,159,819, but due to a technical error actually totaled 1,043,689. The recommended changes above correct these errors.

** The appropriation to the Colorado Immunization Program is divided between CDPHE and HCPF, with $1,375,175 going to CDPHE and $171,251 going to HCPF.

Does JBC staff believe the request meets the Joint Budget Committee's supplemental criteria? [An emergency or act of God; a technical error in calculating the original appropriation; data that was not available when the original appropriation was made; or an unforseen contingency.]	**YES**
This supplemental is the result of *data that was not available when the original appropriation was made.*	

Department Requests: The Departments that administer tobacco-settlement-supported programs have not requested this supplemental.

Background and Analysis: These supplemental adjustments to appropriations are required for two reasons:

1. The appropriations to most tobacco-settlement-supported programs are based on settlement revenues received during the prior fiscal year. The appropriations in the FY 2008-09 Long Bill were based on a forecast that the state would receive $106.7 million of tobacco settlement payments during FY 2007-08. Actual FY 2007-08 receipts turned out to be $3.0 million lower than expected.

2. The appropriations to Tier 2 tobacco programs depend, in part, on the appropriation to the state's Home- and Community-based Services for Children with Autism Program, which, pursuant to statute, must receive an appropriation that covers the program's needs. The appropriations in the FY 2008-09 Long Bill were based on a forecast that the autism program would require an appropriation of $500,000. Staff now forecasts that the program will require an appropriation of $900,000.

Statutory rules prescribe how settlement revenues are allocated among settlement-supported programs. In most cases, the Treasury divides settlement moneys among the various cash funds that support most tobacco-settlement programs, and the General Assembly then appropriates the allocated moneys from these cash funds to the respective programs. Without such appropriations, the programs can't spend the settlement money that they have been allocated. These appropriations depend in whole or in substantial part upon the amount allocated.

Normally at this point, staff would cover the funding rules for tobacco-supported programs quickly, referring the Committee to an appendix for detail. However, under the current economic circumstances, staff believes that it is wise to now go over the key tobacco-settlement funding rules more explicitly. These rules provide important background for subsequent parts of this document and will help the Committee better understand some of the Departmental requests that other analysts will present during later supplementals.

Programs Funded with Tobacco Settlement Payments
FY 2008-09 Supplemental Recommendation
JBC Working Document - Subject to Change

Funding Rules for Tier 1 and Tier 2 programs. Section 24-75-1104.5, C.R.S., divides settlement-supported programs into two categories which are often referred to as "Tier 1" and "Tier 2" programs. The amount allocated to most Tier 1 programs in a given fiscal year depends upon total settlement payments received during the prior fiscal year. (Note that this is a simplification that ignores the accelerated use of $15.4 million of tobacco-settlement revenue that was established by H.B. 07-1359.)

Table 1 lists the Tier 1 settlement programs and provides a somewhat simplified summary of each program's current statutory funding rules. The "Added to Statute" column shows when the program started receiving tobacco funding, though in many cases the original funding formula has subsequently been changed. If the Committee wants to alter appropriations to tobacco-settlement programs to respond to the current economic downturn, it will need to compare programs, and one relevant consideration when comparing is the length of time that a program has been funded with settlement dollars.

Table 1

Tier 1 Program	Added to Statute by	Portion of the prior-year settlement payment allocated to the program or to the program's cash fund
Comprehensive Primary and Preventive Care Grant Program	S.B. 00-071	3%, up to a maximum of $5 million
Children's Basic Health Plan	S.B. 00-071	24%, up to a maximum of $30 million
Nurse Home Visitor Program	S.B. 00-071	13% in FY 2008-09 up to a maximum of $19 million. The percentage rises to 14% in FY 2009-10, 15% in FY 2010-11, etc., topping out at 19% in FY 2014-15.
Read-to-achieve Grant Program	S.B. 00-071	5%, up to a maximum of $8 million
State Veterans Trust Fund	S.B. 00-071	1%, up to a maximum of $1 million, is allocated to the Trust Fund. A statutorily established portion of this allocation is then expended by the Department of Military and Veterans Affairs
Fitzsimons Lease Purchase	S.B. 00-071 & H.B. 03-1256*	8%, up to a maximum of $8 million
Dental Loan Repayment Program	S.B. 01-164	$200,000 annually (not tied to the prior-year payment)
Child Mental Health Treatment Act Program	S.B. 03-282	$300,000 annually (not tied to the prior-year payment)
State share of funding required for Home- and Community-based Services for Children with Autism Act	S.B. 04-177	Enough to fund program needs, up to $1 million (not tied to the prior-year payment)

Tier 1 Program	Added to Statute by	Portion of the prior-year settlement payment allocated to the program or to the program's cash fund
Ryan White HIV/AIDS Drug Assistance Program	H.B. 04-1421	3.5%, up to a maximum of $5 million
Tony Grampsas Youth Services Program	H.B. 04-1421	4%, up to a maximum of $5 million
HIV and AIDS Prevention Grant Program	H.B. 06-1054	2%, up to a maximum of $2 million

*S.B. 00-071 directed 8% of the tobacco settlement money to the University of Colorado for Tobacco and Substance Abuse Research Grants. H.B. 03-1256 redirected this money to support the lease purchase agreement at Fitzsimons.

Actual appropriations of settlement moneys to Tier 1 programs closely track the allocation of settlement dollars prescribed in the above table, though these appropriations sometimes deviate modestly due to the presence of a cash fund that supports a program. These cash funds serve as buffers between the allocation and the appropriation.

The allocations in Table 1 do not utilize 100 percent of the prior-year settlement payment. The remainder, which is sometimes called the "Tier 2 Amount", is allocated among Tier 2 programs in the following percentages:

Table 2

Tier 2 Program	Added to Statute by	Percentage
University of Colorado Health Sciences Center	S.B. 07-97	49.0%
Mental Health Services for Juvenile and Adult Offenders	S.B. 07-97	12.0%
Comprehensive Primary and Preventive Care Grant Program	S.B. 07-97	8.5%
Local Public Health Services	S.B. 07-97	7.0%
Increase Children's Basic Health Plan Eligibility from 200% to 205% of the Federal Poverty Level	S.B. 07-97	5.0%
Supplemental State Contribution for Group Benefit Plans	S.B. 07-97	4.5%
Colorado Immunization Program	S.B. 07-97	4.0%
Alcohol and Drug Abuse	S.B. 07-97	3.0%
Short-term Grants for Innovative Health Programs	S.B. 07-97	6.0%
Medicaid Shortfalls at Children's Hospital	S.B. 07-97	1.0%
Total		**100.0%**

Note that these allocations utilize 100 percent of the remaining settlement payments. Also note that Tables 1 and 2 have ignored small appropriations to the State Auditor's Office and to the Department of Public Health and Environment's Administration division.

As noted above, the autism appropriation depends upon program need. If this appropriation is below the $1 million ceiling and program need change by the time of supplementals, the resulting supplemental adjustment to the appropriation will change the amount available to Tier 2 programs, which in turn will drive supplemental adjustments to the appropriations to nine of the ten Tier 2 appropriations. The timing of these supplemental appropriations is troublesome because the information on which the autism supplemental should be based does not become available until mid February, after the supplemental bills for the various agencies of state government have been introduced. Note that this late-arriving information was not a problem when S.B. 04-177 added the appropriation to statute because there were, at that time, no Tier 2 programs; tobacco settlement revenues that were not allocated to Tier 1 programs at that time flowed to the General Fund.

Long Bill appropriations are based on settlement-revenue forecasts. Once actual payments are known, a supplemental is often needed. Because most of the appropriations in the Long Bill to settlement-supported programs depend upon the amount of settlement revenue received in the prior fiscal year, and because the April payment is not known at the time the Long Bill is written and approved, each year's Long Bill must be based upon a forecast of settlement payments, a forecast that almost always proves incorrect. Supplementals are then required the following January to correct resulting inaccuracies.

Thus the $3.0 million error in the settlement revenue forecast on which FY 2008-09 Long Bill appropriations were based requires that many, but not all, of the appropriations to settlement-supported programs in the FY 2008-09 Long Bill be adjusted.

Staff Recommendation: Staff recommends that the Committee adopt the FY 2008-09 appropriation adjustments indicated in the above table. The recommendations in the above table fall into three categories:

1. Recommendations that are completely specified by statute. In these cases, staff has recommended the required mechanical adjustment to the appropriation.

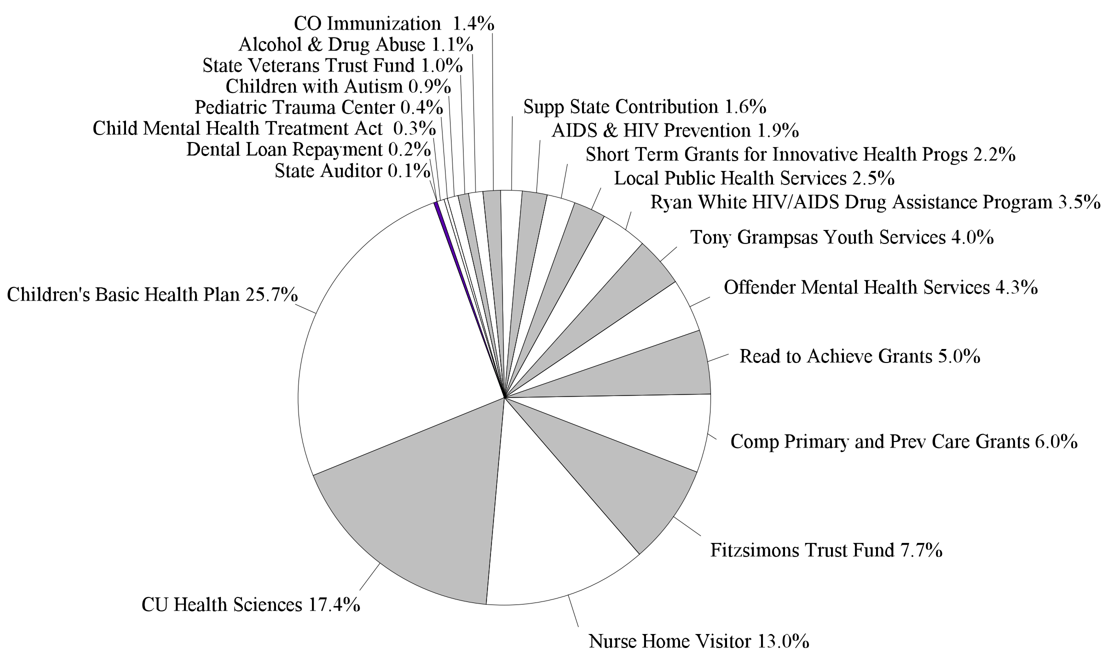
2. Recommendations for which statute provides modest flexibility regarding the appropriation. In cases in which a given settlement program is not assigned to this staff member, the assigned staff member was asked to make a recommendation and that recommendation is reflected above.

3. Recommendations that this staff member prefers to defer to the staff member who handles the assigned program. These staff members will present the recommended adjustments later, when they present supplementals for their departments.

These adjustments are required by current law and should be adopted whether or not the Committee decides to sponsor bills to change the tobacco statutes. The Committee cannot assume that bills it sponsors will become law.

The following pie chart shows the allocation of the FY 2007-08 settlement payments among supported programs.

Allocation of Settlement Payments for Expenditure in FY 2008-09



Part 2
Recommended Statutory Changes to Tobacco Supported Programs

In this section, staff will discuss various ways that tobacco settlement programs could be used to respond to the current economic downturn.

Historical Background: Normally during supplementals, staff would not even mention the history of the Master Settlement agreement, which brought tobacco-settlement moneys to Colorado. But under the current economic circumstances, staff believes that a brief history may help the Committee develop criteria that can be used to support decisions relating to tobacco programs.

In the mid 1990's, various states began suing the major tobacco companies to recover Medicaid and other health-care costs that they had incurred as a result of smoking-related diseases. The states also made other claims, asserting for example that tobacco companies violated consumer protection and antitrust laws, targeted children and teenagers with their marketing efforts, withheld information about the adverse health effects of tobacco, and manipulated nicotine levels to maintain smokers' addictions. However, there is no question that the most important component of these lawsuits was the assertion that states had, through their Medicaid and health programs, incurred large costs from smoking-related illnesses.

Following separate 1997 settlements with Mississippi, Florida, Texas, and Minnesota, and an abortive 1997 effort at a far-reaching global settlement with the remaining states that would have required Congressional action, the tobacco industry and the remaining states agreed to the Master Settlement Agreement in November 1998. In the agreement, the participating tobacco manufacturers agreed to

1. Abide by a variety of public health restrictions on the advertising and marketing of cigarettes,
2. Create and fund the American Legacy Foundation, which conducts youth-targeted anti-tobacco advertising, and
3. Make specified payments to the settling states *in perpetuity*.

In return, the settling states agreed to release the participating manufacturers from health-related claims by the states and their local governments related to the use, manufacture and marketing of tobacco products.

The Recitals at the beginning of the Master Settlement Agreement, declare that the states entered into the agreement to further their policies regarding public health, including policies to reduce underage tobacco use. The Recitals include the following statement, which provides the agreement's only indication as to how the states might spend their settlement moneys:

> WHEREAS, *the Settling States and the Participating Manufacturers* wish to avoid the further expense, delay, inconvenience, burden and uncertainty of continued litigation (including appeals from any verdicts), and, therefore, *have agreed to settle their respective lawsuits and potential claims pursuant to terms which will achieve for the Settling States and their citizens significant funding for the advancement of public health, the implementation of important tobacco-related public health measures, including the enforcement of the mandates and restrictions related to such measures,* as well as funding for a national Foundation dedicated to significantly reducing the use of Tobacco Products by Youth...the Settling States and the Participating Manufacturers...memorialize and agree as follows

(The "national Foundation" in this recital is the tobacco-industry-funded American Legacy Foundation, mentioned earlier.)

The agreement imposes no spending restrictions upon the states; it does not require settlement payments to be spent on anti tobacco programs, on smoking-related health programs, or on health programs of any kind. However, the basis on which the states undertook their lawsuits and the Recitations in the agreement may be reasonably interpreted to imply that the states planned to spend settlement payments on anti-smoking and public health measures.

Creation of the Tobacco Litigation Settlement Trust Fund. The General Assembly could not reach consensus during the 1999 session over how the new tobacco revenues should be spent, but it did decide that a portion of the revenues should be permanently set aside in the Tobacco Litigation Settlement Trust Fund. This decision indicated that the General Assembly is willing, under the right circumstances, to defer the use of a substantial amount of General fund revenue for an extended period of time, a fact that staff will return to later. Senate Bill 99-231, which created the Trust fund, deposited the first $33 million of settlement payments the fund and required that 20% of each subsequent payment be deposited to the Trust fund. The bill added the Section 24-22-115.5 (1), C.R.S., to statute, which declared:

> (1) The general assembly hereby finds and declares that:
>
> (a) The purpose of the tobacco litigation settlement trust fund created by this section is to provide a permanent source of tobacco litigation settlement moneys so that all programs or funds authorized by law to be funded with tobacco litigation settlement moneys can be fully funded without appropriations of general fund moneys; and
>
> (b) It is the intent of the general assembly that all interest derived from the deposit and investment of moneys in the tobacco litigation settlement trust fund be retained in the trust fund until such time as actuarially sound projections of future interest earnings

indicate that the interest to be derived from the deposit and investment of moneys in the trust fund will be sufficient to fully fund any programs or funds authorized by law to be funded by tobacco litigation settlement moneys.

During the 2001-2003 economic downturn, the Trust fund was one of the first places that the General Assembly looked as it sought to prop up the General Fund. The above declaration remains in statute to the current day, though the Trust Fund currently has no balance and receives no funding.

The 2000 session produced S.B. 00-71, which began allocating settlement payments to programs and directed remaining settlement payments into the Trust Fund. In FY 2000-01, 65% of settlement revenues went to programs and 35% went into the trust. The session also produced S.B. 00-74, which specified that the attorney fees received by the state from the tobacco settlement be deposited into a newly created Defense Account of the Tobacco Litigation Cash Fund. The attorney fees were then subject to appropriation by the General Assembly for the purpose of defending the state in disputes stemming from the Master Settlement Agreement.

Tobacco and the 2002 to 2003 economic downturn: The prior economic downturn began after the September 2001 attacks and, during the 2002 and 2003 sessions, produced a number of JBC bills that were designed to support the General Fund, including several bills that involved tobacco settlement payments.

2002 Session: The JBC's 2002 session bills used tobacco revenues that had accumulated in the Tobacco Litigation Settlement Trust Fund and the Defense Account of the Tobacco Litigation Settlement Fund, to support the General Fund:

- House Bill 02-1445 and H.B. 02-1478 authorized the Governor to transfer the balance of the Tobacco Trust Fund to the General Fund at the end of the fiscal year if General Fund revenues fell short of that required to balance the budget and maintain a two percent General Fund reserve. At the end of the fiscal year, the Governor utilized this authority to transfer $138 million to the General Fund.
- House Bill 02-1391 transferred $3.5 million from the Tobacco Settlement Defense Account to the General Fund and provided for subsequent repayment of the Defense Account by the General Fund.

The General Assembly did not cut spending by tobacco-settlement programs during the session; the appropriations approved during the session followed the statutory formulas.

2003 Session: The JBC's 2003 session bills continued the tobacco transfers, moving a further $6.3 million from the Trust Fund to the General Fund while transferring $2.2 million from the State Veterans Trust Fund and $2.0 from the Children's Basic Health Plan Trust Fund to the General Fund.

During the session the General Assembly also began reducing appropriations to settlement programs, first with a set of statutory changes in S.B. 03-190 that reduced the FY 2002-03 appropriations to settlement programs, which had equaled $77 million, by $11 million, a 15 percent reduction that programs had to absorb over the course of five months. This was followed by a second round of statutory changes in S.B. 03-282 that cut an additional $5 million from FY 2002-03 appropriations to settlement programs. Senate Bill 03-282 also contained statutory changes that reduced FY 2003-04 appropriations to settlement programs by approximately a quarter, relative to the appropriations they would have received under preexisting law. These reductions were not equally distributed; Read-to-Achieve appropriations fell 43 percent while appropriations to the Tobacco Education, Prevention, and Cessation Grant Program appropriation fell 74 percent. This bill also provided $2.5 million of temporary tobacco-settlement funding for half a dozen programs that had not formerly received settlement money and, with the exception of child mental health treatment, have not subsequently received tobacco funding. (The Regional Library Service System, the Council on the Arts, the Child Mental Health Treatment Act, the Mental Health Capitation Program, Family Violence Grants, and Juvenile Diversion Programs). The net savings from these two bills, which affected both FY 2002-03 and FY 2003-04 appropriations were transferred to the General Fund to support *FY 2002-03* General Fund Expenditure. This perhaps surprising result is a consequence of the timing of the receipt of tobacco settlement revenues, which staff will elaborate upon shortly.

Finally, concern that the state might run out of cash after the end of the 2003 session led the General Assembly to enact S.B. 03-268 which gave the State Treasurer, the Director of OSPB, and the State Controller standby authority to sell or "securitize" up to 60 percent of the state's tobacco settlement payment stream to raise $160 million for a cash flow reserve, if needed. Securitization proved unnecessary and this authority expired unused.

2004 Session: By the time the 2004 session began, General Fund revenues had started to recover, though the JBC still had to deal with the lingering effects of the downturn. The result was H.B. 04-1421, a JBC bill that effectively suspended the deposit of settlement payments into the Tobacco Litigation Settlement Trust Fund for four years and directed them into the General Fund. The bill also added the Colorado HIV and AIDS Assistance program and the Tony Grampsas Youth Services program as recipients of settlement moneys, slowed the statutorily-mandated grow of the Nurse Home Visitor program, halved the Comprehensive Primary and Preventive Care Grants Program's tobacco settlement allocation, cut the Read-to-achieve program, and made permanent the prior session's allocation of settlement money for child mental health treatment.

Observations. This review of the relevant history of Colorado's tobacco programs leads to the following observations.

1. **Changes to tobacco settlement programs require bills.** All changes to tobacco-settlement programs, except adjustments that true-up appropriations so they align with statute (like those

recommended in Part 1 of this document), require statutory change. Statutory change is also required for all cash fund transfers, including those involving tobacco-settlement money. However, should the Committee seek such change, it will probably be possible to consolidate the changes into a small number of bills, such as a tobacco bill for supplementals and a tobacco bill for figure setting.

2. **The post-recovery consequences of statutory change should be anticipated.** House Bill 04-1421 effectively suspended the deposit of settlement payments into the Tobacco Litigation Settlement Trust Fund for four years and directed them into the General Fund. As the economy recovered in FY 2004-05 and subsequent years this had an effect that some members of the General Assembly may not have foreseen: the diversion added to the year-end General Fund reserve and increased the H.B. 02-1310 allocation of excess general fund surplus to the HUTF and to capital construction.

3. **Delay makes adjustment more difficult.** It's well known that it is more difficult for a program to absorb a 10 percent mid-year reduction than it is to absorb an equal cut enacted before the fiscal year begins. Had the JBC and the General Assembly foreseen during 2002 figure setting the mid-year reductions to FY 2002-03 enacted during the 2003 session, the reductions would have been more easily absorbed.

4. **If the current recession is as deep as the last one, cuts to tobacco-supported programs are likely.**

5. **Securitization is no longer a viable option.** The General Assembly provided standby authority for securitization of tobacco revenues in FY 2003-04 to deal with a potential cash crunch, but this is probably not a workable plan for the current downturn. Iowa, which raised $800 million by securitizing a portion of its tobacco payments in 2005, recently tried to sell the rights to more of its future tobacco settlement payments. Iowa's legislature authorized a second securitization as long as the bond sale could raise at least $183 million. After exploring the securitization market, the Iowa state treasurer concluded that securitization would raise no more than $130 million – 71% of the expected amount. The state shelved the plan.[1]

   A recent *Wall Street Journal* article on the municipal bond market highlighted the currently depressed prices of tobacco-backed bonds, such as those that Iowa sought to sell. The article stated that Oppenheimer's Rochester National Municipal Bond Fund tops Morningstar's list of the worst high-yield municipal bond fund performers in 2008, with losses of 49%. The

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[1] *Chicago Tribune*, December 11, 2008.

decline is in substantial part due to the fund's investments in tobacco bonds.[2]

Forbes reports that a December U.S. Supreme Court ruling that allows tobacco companies to be sued under state law for deceptive advertising of "light" cigarettes has depressed tobacco bonds by making them a riskier investment.[3]

6. **Reduced FY *2009-10* appropriations to tobacco-settlement programs can support increased FY *2008-09* General Fund appropriations.** During the 2003 session, the General Assembly cut appropriations to *FY 2003-04* appropriations in order to increase *FY 2002-03* General Fund spending. This worked because, at that time, tobacco-settlement programs spent settlement revenues with a one fiscal-year lag. This meant that a $1 million reduction in FY 2003-04 appropriations to settlement programs at the time of figure setting, coupled with a $1 million transfer of settlement money to the General Fund during FY 2002-03, boosted FY 2002-03 General Fund revenue and potential FY 2002-03 appropriations by $1 million.

   Today, some 85 percent of the state's tobacco revenues are spent with a one fiscal-year lag; due to changes wrought by H.B. 07-1359, the remaining 15 percent are spent in the year received. However, the 85 percent that is still spent in the subsequent year allows the Committee to continue to use this technique.

7. **Decreased FY 2008-09 appropriations of tobacco-settlement dollars to tobacco-settlement programs, coupled with equal increases in General Fund appropriations to the same programs will increase spending subject to the 6 percent limit while leaving the total appropriations to the programs unchanged.** This technique, which appears not to have been used with tobacco revenues during the last economic downturn, is best illustrated with examples.

   Example, AIDS Drug Assistance: The FY 2008-09 appropriation to the Department of Public Health and Environment's AIDS Drug Assistance program is $1.3 million General Fund, $3.7 million cash funds from tobacco-settlement revenues, and $8.3 million Federal Funds. If the General Assembly reduced this program's cash funds appropriation by $1 million, transferred the savings to the General Fund, and then increased the program's General Fund appropriation by $1 million, expenditures subject to the 6 percent limit would rise by $1 million without changing the program's total spending. This could potentially be a useful

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[2] *Wall Street Journal*, December 23, 2008.

[3] www.forbes.com/afxnewslimited/feeds/afx/2008/12/15/afx5823179.html

change if the Committee concludes that Colorado will be unable to appropriate to the 6 percent limit this year.

Example, The Supplemental Appropriations and Overexpenditures Account: House Bill 07-1359 diverted $24.4 million of FY 2006-07 tobacco settlement payments into the Health Care Supplemental Appropriations and Overexpenditures Account of the Tobacco Litigation Settlement Cash Fund. The remaining balance in this account equals $10.5 million and some portion of this $10.5 million is likely to be expended in FY 2008-09. If a $1 million expenditure is first transferred to the General Fund and then expended, General Fund expenditures subject to the 6 percent limit will rise by $1 million.

Example, The Fitzsimons lease-purchase: The Fitzsimons lease-purchase agreement is supported in part with an $8 million FY 2008-09 appropriation of tobacco-settlement dollars. If the General Assembly reduced this appropriation by $1 million, transferred the savings to the General Fund, and then increased General Fund appropriation for the Lease Purchase by $1 million, expenditures subject to the 6 percent limit would rise by $1 million without changing the program's total spending.

Example, Children's Basic Health Plan Expenditures: The Children's Basic Health Plan will receive $26.7 million of tobacco-settlement dollars during FY 2008-09. If the General Assembly reduced this appropriation by $1 million, transferred the savings to the General Fund, and then increased General Fund appropriation for the plan by $1 million, expenditures subject to the 6 percent limit would rise by $1 million without changing the program's total spending.

Possible modification to CDPHE's AIDS Drug Assistance supplemental request: As noted above, the FY 2008-09 appropriation to the Department of Public Health and Environment's AIDS Drug Assistance program is $1.3 million General Fund, $3.7 million cash funds from tobacco-settlement revenues, and $8.3 million Federal Funds. In its supplemental budget request CDPHE, has proposed a $65,000 one-time reduction in the General Fund appropriation to this program. If the reduction instead came from the program's tobacco settlement appropriation, total program spending would fall by the same amount but General Fund appropriations would not decline.

Possible modification to CDPHE's Local Public Health supplemental request: The FY 2008-09 appropriation to the Department of Public Health and Environment for distributions to local public health departments is comprised of $6.0 million General Fund and $2.7 million of cash funds from tobacco settlement revenues. The Department's FY 2008-09 supplemental budget request proposes to reduce the cash funds appropriation by $149,070. If the reduction instead came from the program's tobacco-settlement appropriation, total program spending would fall by the same amount but General Fund appropriations would not decline.

Possible modification to a supplemental request for the University of Colorado: The Colorado Commission on Higher Education has requested that the FY 2008-09 appropriations to higher education institutions, including the University of Colorado, be reduced by a total of $30 million. As indicated in Part 1 of this document, the CU health sciences center has a FY 2008-09 appropriation of $18.9 million of settlement revenue. In order to support spending subject to the 6 percent limit, the Committee may wish to reduce CU's appropriation of tobacco-settlement dollars, rather than cut its General Fund appropriation.

More complete presentations concerning these possible modifications to departmental requests will be made by during the supplemental presentations for the Departments of Higher Education, Health Care Policy and Financing, and Public Health and Environment.

8. **The Tobacco Litigation Settlement Trust Fund is no longer available to cushion a downturn.** The Trust fund supported the General Fund in two ways during the last downturn: (1) the approximately $138 million balance that it had accumulated during prior years was transferred to the General Fund, and (2) settlement revenues that would have gone to the Trust Fund during the downturn were redirected to the General Fund. However, the Trust Fund no longer has a balance and no longer receives revenues.

9. **Other cash funds that receive tobacco revenue are potential sources for transfers.** During the last economic downturn, the General Assembly transferred balances from the Defense Account of the Tobacco Litigation Cash Fund and the State Veterans Trust Fund to the General Fund. Both still exist and have substantial balances. They have been joined by two other funds with balances large enough to serve as sources for transfers to the General Fund: the Short-term Innovative Health Program Grant Fund and the AIDS and HIV Prevention Fund.

   The Department of Veterans and Military Affairs has requested a $4.6 million transfer from the State Veterans Trust Fund to the General Fund and the Department of Public Health and Environment as requested a $4.3 million transfer from the Short-term Innovative Health Program Grant Fund. **More complete presentations concerning these transfers will be made during the supplemental presentations for the Departments of Law, Military Affairs, and Public Health and Environment.**

Staff Recommendation: Abolish several tobacco settlement programs and make minimal cuts in the remaining programs. The policy options examined above leave intact the existing network of tobacco-settlement programs. The transfers to the General Fund would help the State avoid some modest General Fund cuts. Other options would prop up appropriations subject to the 6 percent limit without providing any extra overall funding. However, these options will not help the state live within a General Fund budget that may grow along a permanently lower trajectory following the downturn, nor will they help the state deal with the next, inevitable recession.

Impressed by the willingness of the General Assembly during the 1999 and 2000 sessions to defer the use of tobacco settlement revenues for an extended period of time and impressed by the way in which the Tobacco Litigation Settlement Trust Fund helped cushion the last economic downturn, which would have seen more than $150 million of extra General Fund appropriation reductions without the Trust fund, **Staff recommends that the Committee consider more fundamental change to the tobacco statutes. Specifically, staff recommends that the Committee introduce legislation to permanently abolish several tobacco programs and use the resulting savings to create a modest rainy day fund that would only be used in the event of a recession. This fund would be used during the current downturn to support General Fund spending, sparing other settlement-supported programs from cuts, and after the recession is over it would accumulate settlement dollars and interest until the next recession.**

Members of the General Assembly have frequently acknowledged the value of a rainy day fund, and some who hesitated may now wish secretly, or perhaps not so secretly, that something had been set aside in prior years. If the Committee sponsored legislation that reduced tobacco-settlement appropriations enough to free $10 million annually for a rainy day fund, the state would have approximately $50 million set aside, plus interest, each time a downturn occurs, assuming that a recessions happens once every 5 to 6 years, as they have during the post-war era. It's tempting to argue that $50 million is not worth setting aside because it is insufficient to prevent the cuts that inevitably and periodically result from state's current budgeting techniques, but rejecting the recommendation because of its modest size is reminiscent of the individual who threw up his hands in despair when told hold much he needed to save for retirement, saying "I can't possibly save that much, so I won't even try." Perhaps if he tried saving a modest amount, he would find that it was not as difficult as he imagined and he might find himself saving more than he previously thought possible. In addition, staff believes that the benefits of an extra $10 million of spending each year for five years are more than offset by the harm created by an extra $50 million of cuts during a downturn.

Staff recommends that the Committee select several criteria for program evaluation and use those criteria to decide which programs should be eliminated. Specifically, staff suggests the following:

1. **Does the program contribute to the health of Coloradans?** This criteria is consistent with the history of the state's tobacco litigation and with the Master Settlement Agreement's recitals, which explain the reasons for the agreement.

2. **Does the program reduce tobacco use?** Staff would normally rank this as a key criterion, but passage of Amendment 35, which in recent years has provided about $35 million of support for Tobacco Education, Prevention, and Cessation has substantially reduced the importance of this consideration.

3. **Does the program draw a federal match?** Such leverage makes a program more appealing.

4. **Will a cut to the program require a dollar-for-dollar back fill with state funds?** In such cases, elimination of the program makes little sense because the state will need to find an alternative funding source.

5. **Will a cut to the program increase appropriations elsewhere?** This is an often difficult to access criteria.

Other criteria, such as the length of time a program has been in statute are also also of value. The following table applies the above criteria to Colorado's tobacco settlement programs.

Programs Funded with Tobacco Settlement Payments
FY 2008-09 Supplemental Recommendation
JBC Working Document - Subject to Change

	Public Health/ Health Care Program	Draws a federal match	Cuts require dollar-for-dollar back fill with state funds	Cuts may increase approps elsewhere	JBC Staff Comments
Tier 1 Programs					
Read-to-Achieve Grant Program	No	No	No	No	Discretionary Program.
Comprehensive Primary and Preventative Care Grant Program	Yes	No	No	No	Discretionary Program. Cut in funding would decrease amount of funding available for safety net provider grants to maintain or increase health infrastructure but does not impact other state programs immediately. Funding changes to this program could be contained in a Tobacco Master Settlement Fund bill.
Children's Basic Health Plan Trust Fund	Yes	No	Yes	Maybe	All of the fund balance in the Trust Fund is anticipated to be used in FY 2009-10. The Fund is anticipated to have a deficit by the end of FY 2009-10 without additional General Fund appropriations. Changes to the CBHP Program would need separate legislation from a Tobacco Master Settlement Fund bill.
State share of funding required for Children with Autism Act	Yes	Yes	Yes	Maybe	This fund pays for the Autism Waiver Services State Match under the Medicaid Program up to $1.0 million. Program costs are anticipated to be close to $1.0 million beginning in FY 2009-10. Changes to the Autism Waiver Services would need to be made in a bill separate from a Tobacco Master Settlement Fund bill.
Fitzsimons Lease Purchase	Yes	No	Yes	--	
State Veterans Trust Fund	Yes	No	No	No	

PROGRAMS FUNDED WITH TOBACCO SETTLEMENT PAYMENTS
FY 2008-09 SUPPLEMENTAL RECOMMENDATION
JBC WORKING DOCUMENT - SUBJECT TO CHANGE

	Public Health/ Health Care Program	Draws a federal match	Cuts require dollar-for-dollar back fill with state funds	Cuts may increase approps elsewhere	JBC Staff Comments
Child Mental Health Treatment Act	Yes	No	No	No	
Dental Loan Repayment Program	Yes	No	No	No	
HIV and AIDS Prevention Grant Program	Yes	No	No	No	
Ryan White HIV/AIDS Drug Assistance Program	Yes	No	No	No	
Tony Grampsas Youth Services Program	No	No	No	No	
Nurse Home Visitor Program	Yes	Yes	No	Maybe	Medicaid match for many participants.
Tier 2 Programs (Programs created by S.B. 07-97)					
University of Colorado Health Sciences Center	Yes	No	No	No	The proposed supplemental reductions to higher education do not take this appropriation into account. CU receives both General Fund and tobacco settlement money and is above to move these moneys between various uses with few restrictions.

PROGRAMS FUNDED WITH TOBACCO SETTLEMENT PAYMENTS
FY 2008-09 SUPPLEMENTAL RECOMMENDATION
JBC WORKING DOCUMENT - SUBJECT TO CHANGE

	Public Health/ Health Care Program	Draws a federal match	Cuts require dollar-for-dollar back fill with state funds	Cuts may increase approps elsewhere	JBC Staff Comments
Mental Health Services for Juvenile and Adult Offenders	Small Amount	No	No	No	
Comprehensive Primary and Preventative Care Grant Program	Yes	Yes, new federal match program	No	No	The amount of funds that go to Rural and Public Hospital Payments pursuant to 25.5-3-207 (4) (b), C.R.S. (2008) can draw down a federal match. This is a new draw down of federal funds that will be begin in FY 2008-09. The Committee could conceivably reduce the percentage of state funds for this program but maintain the same level of appropriation as originally anticipated for FY 2008-09 because of the addition of the federal funds. This program could also be eliminated or reduced and would not result in a need for additional GF or other state funds to backfill. This is a discretionary program. Reductions to this program could be made in a Tobacco Master Settlement Fund bill.
Local Public Health Services	Yes	No	No	No	
Children's Basic Health Plan Trust Fund Account (increase eligibility from 200% FPL to 205% FPL)	Yes	Yes	Yes		The CBHP Program would require legislation other than the Tobacco Master Settlement Bill in order to reduce costs.
Supplemental State Contribution for Group Benefit Plans	Yes	No	No	No	

PROGRAMS FUNDED WITH TOBACCO SETTLEMENT PAYMENTS
FY 2008-09 SUPPLEMENTAL RECOMMENDATION
JBC WORKING DOCUMENT - SUBJECT TO CHANGE

	Public Health/ Health Care Program	**Draws a federal match**	**Cuts require dollar-for-dollar back fill with state funds**	**Cuts may increase approps elsewhere**	**JBC Staff Comments**
Colorado Immunization Program	Yes	No	No	Maybe	
Alcohol and Drug Abuse	Some	No	No	No	
Short-term Grants for Innovative Health Programs	Yes	No	No	No	This program has barely started operating and has only made a couple of grants.
Medicaid Shortfalls at Children's Hospital	Yes	Yes	No	No	This is a discretionary payment to Children's Hospital. It draws a federal match but if eliminated or reduced would not necessary require GF or other state money to back fill the program. Reductions to this program could be made in an omnibus Tobacco Tax Master Settlement Fund bill.

A straight forward, unweighted application of these criteria would lead the Committee to conclude that the Read-to-Achieve Grant Program, the Tony-Grampsas Youth Services Program, and Mental Health Services for Juvenile and Adult Offenders should no longer receive funding from tobacco settlement revenues. Staff suggests that the Committee also add Short-term Grants for Innovative Health Programs to this list, which is a program that is now operating at a low level and has made few grants. In addition, the Department of Public Health and Environment is requesting that this program be scaled back substantially for the next three years in order to support transfers to the General Fund.

The following table shows the resulting reduction in cash fund appropriations to settlement programs. These savings would, during the recession, be used to support the General Fund and, after the recession, would be allowed to accumulate until the next economic downturn.

	Allocation of Settlement Revenues
Read-to-Achieve Grant Program	$5,174,508
Tony-Grampsas Youth Services Program	4,139,607
Mental Health Services for Juvenile and Adult Offenders	4,419,502
Short-term Grants for Innovative Health Programs	2,209,751
Total	$15,943,368