

# What's in the cards for 2004?



A good poker player will tell you that luck at the card table comes to those who are prepared. The better prepared, the more luck you'll have.

As state leaders continue their three-year-old effort to get their arms around sluggish revenues, trends are emerging during 2004 that decision-makers will need to know in shaping solutions to their states' fiscal problems.

This month, CSG policy analysts and affiliates provide insights into those trends so state leaders will be better prepared.

---

## States' budget picture cloudy

Overall state spending exceeded state revenues between 2001 and the second quarter of 2003, according to the Bureau of Economic Analysis.

The net effect of continuing state revenue shortfalls is that taxpayers could face another round of tax and fee hikes in 2004 and 2005. These could be packaged as part of "tax modernization" efforts across the states.

Proponents of "tax modernization" say it means rewriting state tax codes to more closely fit modern economies, but does not necessarily mean an overall tax increase for taxpayers. Opponents suggest modernization ultimately means taxing things that weren't previously taxed and thus is an overall tax increase for state taxpayers.

The final result will probably be somewhere in the middle. States will add some new taxes and "adjust" some existing taxes. Increasing general sales taxes, increasing personal income taxes for selected brackets, revising estate tax rules, and expanding the tax base to include more services seem likely, at least in a few states. Most states have avoided increasing personal income taxes since 2001.

Any fee and tax increases will be in addition to increases in

other areas that taxpayers began to pay in 2002 and 2003, such as higher local government property taxes, energy price increases, insurance rate increases and college tuition hikes.

Collectively, such initiatives could slow personal income growth for many Americans over the next 24 to 36 months following a period of sluggish personal income growth. The Bureau of Economic Analysis, for example, reports that personal income nationwide grew 3.3 percent in 2001 and only 2.8 percent in 2002. "This was the second consecutive year of slowing growth and the lowest annual growth rate in over 30 years," the bureau reported.

More recently, according to the BEA, personal income nationwide grew 0.8 percent in the second quarter of 2003, the same as in the first quarter and up slightly from the 0.6 percent increase of the fourth quarter of 2002.

And the Census Bureau reported in September 2003 that the nation's official poverty rate rose from 11.7 percent in 2001 to 12.1 percent in 2002 while the median household income nationwide declined 1.1 percent.

—Bill Voit, senior projects director, [bvoit@cs.org](mailto:bvoit@cs.org)

## Rural voters make an impact

This may be a defining year in the development of a unified voice for rural voters and the emergence of a national rural policy.

Rural areas include 80 percent of the United States' land mass and 55 million people but lag behind metro areas in most economic measures. According to the USDA's Economic Research Service, rural areas have higher poverty rates, fewer college graduates, lower average earnings, fewer year round, full-time jobs and more low-skill jobs.

There is a growing demand for a national rural strategy to address these issues. Health and Human Services Secretary Tommy Thompson, for example, identifying a problem with rural health issues, developed the Office of Rural Health Policy. It serves as a clearinghouse on all matters affecting rural hospitals and health care.

The state of Texas responded similarly in 2001 when its Legislature created the Office of Rural and Community Affairs. This office serves as a clearing agency for the state's health, economic and community development programs for rural Texas communities. One of the agency's goals, similar to one of the

charges of the federal ORHP, is to monitor governmental actions for their effect on rural residents.

Do the policy-makers in this country need to pay more attention to rural residents? Polls show that rural residents are even more concerned than urban voters about access to health care, education and the economy. Rural voters also bring conflicting demands to the ballot box including questions about constraints on the growth of agribusiness conglomeration, divergent approaches to international trade policy and distinct opinions on environmental issues. The importance of the rural vote can not be underestimated, and candidates in state and national races are paying attention.

Recently, a re-energized League of Rural Voters, led by Executive Director Neil Ritchie, held a national summit on agriculture and rural life. It was attended by five of the Democratic candidates for president. Any one of the electoral votes of a single rural state could have made Florida's votes inconsequential, a fact not lost on many candidates in state and national elections

— Carolyn Orr, *lead agriculture and rural policy analyst*, [corr@csg.org](mailto:corr@csg.org)

---

## Schools, private sector battle childhood obesity

One year after the U.S. Department of Agriculture and Centers for Disease Control warned Americans about the growing danger to children's health because of increasing childhood and adolescent obesity, federal, state and local policy-makers have stepped up their roles in shaping legislation, regulations and policy addressing the long-term threat obesity poses for the public's health and for states' health infrastructures.

As state legislatures reconvene across the nation this month, they will have ample sources of information and prototypes to use in the battle against obesity.

Dr. Richard H. Carmona, U.S. surgeon general, introduced a new initiative, "Shaping America's Youth." The food and beverage industry also improved its image and role in the school-centered obesity debates by joining forces with several national school organizations to provide guidelines for school vending.

California, Texas and Arkansas passed laws last year prohibiting soda, hard candy and gum sales to elementary children in public schools and to middle school students during breakfast and lunch.

In Florida, Gov. Jeb Bush has convened a task force to study obesity among the state's children and to issue recommendations on improving school lunch programs, physical education pro-

grams and family involvement. Maine legislators created a similar committee last year after tabling a bill to ban candy and soda sales. Maine and other states will reintroduce various school health bills this session.

Last summer, the Coca-Cola Company announced that it would stop marketing to children under age 12, and then in November forged an agreement with key education groups to establish clear guidelines for marketing and selling its products in schools. Kraft Foods Inc. pledged to eliminate all in-school marketing and establish guidelines for advertising and marketing to children to encourage appropriate eating and active lifestyles.

Although anti-commercialism groups like Commercial Alert and Arizona State University's Commercialism in Education Research Unit remain skeptical, National Association of State Boards of Education Executive Director Brenda Welborn said local school and district decision-makers have the power to determine the beverages they will offer in school vending machines, adding that schools need the revenue.

—Charlotte Postlewaite, *chief education policy analyst*, [cpostlewaite@csg.org](mailto:cpostlewaite@csg.org)

# Trends in turbulent times

By Julia Nienaber Hurst

Globalization, federal mandates and growing political polarization will buffet state governments in 2004 as policy-makers grapple with bleak fiscal conditions.

During a recent state leaders policy conference, “Leading in Turbulent Times,” sponsored by The State Government Affairs Council, participants identified economic, policy, political and federalism trends that are expected to emerge this year.

Massachusetts state Rep. Dan Bosley, 2003 CSG chairman, offered examples of the growing impact international issues have on state budgets.

French farmers, for example, send the United States protein concentrate that competes with products from American dairy farmers, said Bosley.

“A recent CSG trip to Mexico revealed that while some Americans are concerned about manufacturers moving to Mexico, Mexican manufacturers say China is becoming increasingly competitive” and could change the face of world business, he said.

## Federalism

“Federal mandates and the increasing costs of elections will also impact budgets,” said Daniel M. Sprague, CSG executive director. “One trend is opting out of presidential primaries in order to save money.”

Colorado, Kansas, Maine, Michigan, North Dakota, Utah and the state of Washington have cancelled primaries for 2004 in cost-cutting moves.

Other spending areas will also be addressed, said William Pound, executive director of the National Conference of State Legislatures. “Medicaid, higher education, K–12 education and corrections account for two thirds of total state spending as a national average,” Pound said. These expenditures, he said, will result in spending reductions on items like state parks and transportation.

Although power between states and the federal government has been relatively balanced in recent years, according to Sprague and Pound, this balance may be tested as 2004 unfolds. Congress, for example, addressed anti-spam regulation after 30 states passed legislation.

In 2004, the cost and implementation of the No Child Left Behind Act are likely to cause further state action on education. Medicaid spending, too, will continue to be influenced by federal action.

## Policy

“Issues surrounding identity and privacy will prevail in 2004,” said Pound. He said states will likely strive to define a

minimum level of verifiable documentation for identity and will likely pursue methods to improve the quality of identity verification and protection. This will begin to address identity theft and will open issues of privacy.

Privacy discussions open doors to many issues, including policy questions surrounding the advancement of technology. “States must become agile and quickly responsive,” said Sprague. The Internet shares information at a new speed and constituents want service via the Web. He suggested that states may need to restructure. Bosley echoed the sentiment, “Our states, our laws and our tax policies, for the most part, reflect the 1950s manufacturing economy with people walking into work downtown. That’s not today’s world and we can’t wish it back into existence.”

## Politics

The political climate defines, to an extent, what policy-makers are able to do or what they will focus on, said Sprague. “The political climate in post-Watergate was quite different than this era of post-September 11,” he said.

“The climate is increasingly partisan entering a less civil era,” Sprague said. “The Pew Center says political polarization may be at its highest.”

Larry Sabato, director of the Center for Politics at the University of Virginia, agreed with Sprague’s assessment.

“This country is as polarized now as it has ever been,” Sabato said.

Between 2000 and 2003, 26 of the 46 governors’ seats up for election had flipped parties, a record since 1900, Sabato said. “So what does that mean?” he asked. “People don’t trust either party so they are switching parties in power as much as reasonably possible.” The nation is polarized, Sabato contended, primarily around social issues, and the parties are also polarized.

He forecast that governing politicians will prioritize social issues in 2004. “The economy, war and peace, scandal, and social issues are the predictors of the presidency,” said Sabato.

As of November, he said, about 15 percent of the population was unemployed or seriously concerned about losing a job. The other 85 percent, he said, will not vote based on what the other 15 percent is experiencing, they will vote on whether they are richer or poorer. He said in the absence of significant scandal, how the ‘war on terror’ is perceived by people in 2004 and social issues will drive elections, and therefore legislative agendas.

— Julia Nienaber Hurst is executive director of the National Lieutenant Governors Association ([www.nlga.us](http://www.nlga.us)), an affiliate of The Council of State Governments.

---

Although power between states and the federal government has been relatively balanced in recent years, this balance may be tested as 2004 unfolds.

---

## The drug reimportation debate

The controversy over prescription drug costs has taken a new turn as governors and mayors seek to import cheaper medicines from Canada to hold down drug costs for the state and local employees, seniors and the uninsured. Meanwhile, other states continue to look at preferred drug lists and bulk purchasing proposals to hold down drug costs.

According to *USA Today*, spending on imported drugs from Canada has grown enormously in the last three years, rising from just a few million dollars to as much as \$800 million in 2003.

While this purchasing has benefited Canadian pharmacies, critics in the United States argue that cheap medicine may come at an unexpected price. The Food and Drug Administration and pharmaceutical manufacturers argue that over-the-border sales are both illegal and risky. Domestic pharmacies are worried about the impact that international and Internet sales will have on their bottom lines.

The cross-border prescription drug trade has been fueled by a number of factors. Double-digit growth in drug costs have forced some employers to drop health care coverage and others to increase the portion that employees pay out of pocket. Unemployment and a poor economic outlook have also played a role, as has increased media coverage of bus trips to Canada and the lower prices for drugs available there.

In response to pressure to lower prescription drug costs, storefronts have sprung up across the country that assist patients in accessing cheaper medicines from Canada. Some states and cities have also announced plans to assist with reimportation of prescription drugs, usually from Canada.

Illinois Gov. Rod Blagojevich released a study in October on the feasibility of a drug importation program for state employees and retirees. According to the report, Illinois could save as much as \$91 million a year and Canadian pharmacy practices are comparable to those in the United States. The report recommended that Illinois contract with a nondomestic pharmacy management vendor, begin with limited implementation and use a primary care pharmacist model, which would allow patients using mail-order services to consult with a pharmacist about their medications.

Gov. Pawlenty plans to help Minnesotans import drugs from Canada. The state will use a Web site to direct state residents to approved Canadian pharmacies with prices negotiated by the state, according to a report in the St. Paul *Pioneer Press*. Co-pays on drugs would be waived for state employees and others using the site. Governors in Iowa, Wisconsin and Vermont are also considering purchasing from Canadian suppliers, despite federal prohibitions.

Congress authorized reimportation in a 1999 bill but required that the secretary of Health and Human Services determine the ability of the FDA to ensure that the medication supply remained safe. Donna Shalala, Health and Human Services secretary under President Clinton, declined to authorize reimportation based on safety concerns, and Bush administration officials have vigorously resisted reimportation proposals based on the same grounds.

A series of recent articles in the *Washington Post* underscores the FDA's concerns. In a year-long investigation, the *Post* doc-



umented many instances of counterfeiting, dilution and safety violations in the current U.S. drug supply, citing that the number of FDA reports of counterfeiting alone had risen from five cases per year in the 1990s to 20 per year since 2000. The *Post* also documented cases of harm that patients had encountered from Internet and international suppliers. A recent FDA report stated that 88 percent of drugs stopped at the border were illegal and unapproved substances in the United States.

State legislatures and governors continue to look to reimportation as a way to decrease prescription drug costs. There are several factors, however, that state officials need to consider:

- **Legality** – FDA Commissioner Mark McClellan has resisted any attempts to weaken the ban on international drug importation. The FDA is cracking down on storefront operations with connections to Canadian suppliers and there is concern that states that pursue reimportation without federal authorization may run afoul of federal authorities.
- **Feasibility** – Potential cost savings need to be evaluated in light of start-up costs and administrative overhead to operate reimportation programs. Some branded drugs are significantly cheaper in Canada than in the United States and others have more moderate price differences. Fluctuating exchange rates, the mix of drugs ordered, the supply chain and other factors can affect the degree of cost savings that states could realize through mail-order or Internet-based reimportation.
- **Safety** – Some analysts argue that control over the drug supply will be weakened and its safety difficult to protect if reimportation is instituted. Criminals and terrorists could take advantage of operating outside of the United States and introduce counterfeits, diluted or toxic substances to customers in this country.
- **Liability** – If states are involved in brokering arrangements with Canadian suppliers and encouraging the cross-border trade, some analysts warn that states may be open to liability if safety is compromised.

—Trudi Matthews, associate director for health policy, [tmatthews@csg.org](mailto:tmatthews@csg.org)