# Rhode Island 2010

## Charting a New Course

### Demographic Challenges to Affordable Public Services

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October 2005

## I. Introduction

This RIPEC publication – *Rhode Island 2010* - builds on recent RIPEC work to develop research that will further detail the impact selected demographic trends have on the Rhode Island State Budget. RIPEC has developed forecasts through 2010 for different demographic and economic factors that are incorporated into this analysis. There are certain socio-economic factors that influence eligibility for entitlement programs, education services and other programs, and the projected growth in many segments of Rhode Island's population will have an impact on the resources needed to provide quality services. Additional information regarding forecasting methods is available upon request.

This report outlines

- What Rhode Island might look like by 2010;
- What services will be needed to meet projected needs;
- Who will bear the greatest burden to finance these programs; and
- What needs to be done to address identified problems.

In addition to the Introduction, this report is divided into five parts:

**II. Executive Summary**

**III. RIPEC Comments**
This section focuses on the key themes that have emerged from the analysis included in the report and what issues the State will likely face through the remainder of the decade. The section focuses on the need to begin addressing some key issues rather than to muddle through and postpone tough decisions to bring the State's spending habits in line with overall economic activity.

**IV. Demographic Patterns**
This section provides an overview of different age cohorts and projects them out until 2010. In addition, it shows the current level of entitlement recipients, especially related to Medicaid and FIP/child care and the projected level in 2010, number of elderly, and current and projected enrollment in K-12 public schools.

**V. Selected Measures of Income and Residential Property Wealth**
The analysis will include an income profile of Rhode Island in terms of personal income, median family income and housing prices.

**VI. Five-Year Forecast**
Based on RIPEC's demographic, economic and financial analysis, this section provides an overview of current and projected state and local revenues and expenditures, and forecasts operating deficits through the end of the decade. This section also shows projected spending levels for Medicaid, and the Family Independence Program/child care.

## II. Executive Summary

This RIPEC publication – Rhode Island 2010 is a new RIPEC publication that highlights key demographic trends that should be considered when looking at future demands on State and local budgets through the balance of this decade.

**Major Findings**

By 2010, demographic data point towards a Rhode Island that will be older, have fewer workers in their prime productive years, be less self-sufficient and more reliant on government assistance, requiring continued taxpayer investment in entitlement programs and fundamental public services. These trends can affect the State's tax competitiveness and the State's overall economic health, which could translate into higher taxes and an inability to provide affordable public services to Rhode Islanders.

- RIPEC projects annual operating deficits of nearly $145.0 million throughout the balance of the decade, with spending growth outpacing both inflation and personal income growth.

- Social service programs are projected to consume nearly $0.45 of every new $1.00 spent. By 2010, Medicaid will continue to be a major driver, projected to grow by 8.2 percent annually for the remainder of the decade. RIPEC projects that one in five Rhode Islanders will participate in Medicaid by 2010.

- RIPEC projects a 7.5 percent decline in the State's 35-49 population (prime earning years) between 2000 and 2010. RIPEC also projects declining public school enrollments in the State's, and as reported by Cities Count, one in five of the State's workforce in 2020 will have come from the State's urban core school systems, which currently have a high concentration of poor performing schools. Absence of a skilled and growing work force may become a barrier for future investment.

- Over the past five years, the State's median housing price has experienced an average annual growth rate of 14.3 percent. If housing prices in the Ocean State grow at an average annual rate of 6.0 percent for the remainder of the decade, the estimated median price would be $386,000 by 2010.

- RIPEC projects Rhode Island's personal income will grow at an average annual rate of 4.0 percent during the forecast period. In 2000, 8.0 percent of the Federal income tax filers in Rhode Island (those earning $100,000 or more) provided 56.8 percent of the total Federal income tax burden collected in Rhode Island. By 2010, RIPEC projects that those earning $100,000 or more will represent 12.0 percent of all filers but 65.6 percent of the Federal (and therefore State) income tax burden in the State. Thus, the State will rely on fewer income taxpayers to support the spending for these demands.

*Rhode Island 2010* indicates that the State will be facing difficult fiscal and economic challenges for the remainder of this decade. Issues such as State operating deficits, continued demands on Medicaid, school spending growth despite marginally declining enrollments, escalating property tax burdens and a limited housing supply will have an impact on the quality of life in Rhode Island's neighborhoods and communities and raises some pressing questions:

- Will there be enough "Gas" in the state's economic engine to sustain spending habits?
- Can we field a highly skilled workforce?
- How will school spending demands, high property tax burdens and growing housing prices impact the State's quality of life?
- Is entitlement reform possible?

Tackling these issues will take considerable political will, courage and determination. Achieving reform will require new tools and informed public input to help decision-makers focus on choices, cost and benefits and tax competitiveness. Options that are discussed in the Comments section of this report are Tax and Expenditure Limitations and entitlement reform. Properly designed, these options may provide opportunities to make State and local governments more efficient and effective, and provide high quality affordable public services for the citizens of Rhode Island.

## III. RIPEC Comments

Rhode Island 2010 – Charting a New Course – provides insights into how demographic and economic trends have and may impact State and local spending decisions and resulting tax burdens. Demographic data point towards a State that will be older, have fewer workers in their prime productive years, be less self-sufficient and more reliant on government assistance, requiring continued taxpayer investment in entitlement programs and fundamental public services. If Rhode Islanders wish to protect the basic public services we currently enjoy given limited resources, it will be essential to enhance the State's fiscal discipline.

This report highlights key demographic trends that should be considered when looking at future demands on State and local budgets through the balance of this decade. For example, Medicaid demands, combined with growing elderly populations, represent the largest influence on future State budgets. An aging state and local workforce also places considerable pressure on public finances given pension and health care demands. The projected decline in the number of workers in key age cohorts suggest limitations in attracting and retaining private investment.

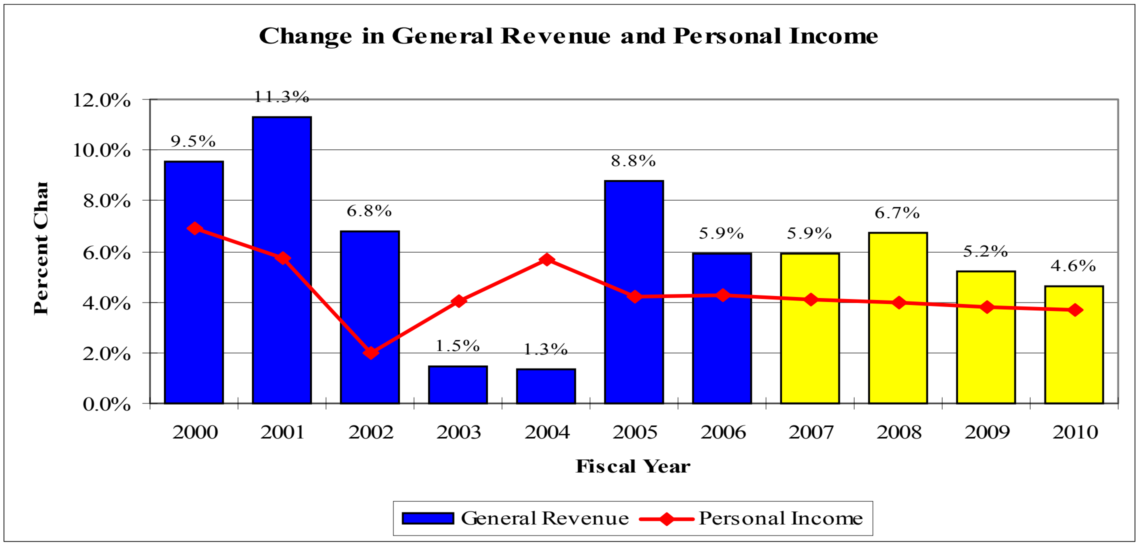
Given these demographic changes and past budget decisions, the State may be heading towards uncertain fiscal times. On one side is the impact demographic changes will have on public finances and how our government will raise revenues to fund these and other services. On the other hand, the State will rely more on fewer income taxpayers and gaming to support current spending habits, and by default, depend more on already high property taxes to support public schools. The result will be higher tax burdens, and when this is combined with the growth in the price of housing, the State may become less attractive to potential higher skilled workers.

The bottom line is that State spending has grown faster than both inflation and personal income. History shows that spending is limited only by the revenues generated in a given fiscal year. These symptoms further undermine the State's tax competitiveness and the State's overall economic health, which could translate into an inability to provide affordable, necessary public services to Rhode Islanders.

The information presented in Rhode Island 2010 suggests that the State is at a critical crossroad, and decisions that are made (or not made) within the next three years will have a profound affect on the future of the Ocean State, our children and grandchildren. Now is the time to consider transformational change.

**Will there be Enough "Gas" in the State's Economic Engine to Sustain Spending Habits?**

Since FY 2000, the State's general revenue budget has grown faster than both inflation and personal income, and is projected to continue to do so through the remainder of the decade. What this means is that State general revenue spending trends show government consuming a greater portion of the State's economy. This translates into increasing burdens on Rhode Islanders to support basic services and other programs while still managing their own budgets. Furthermore, RIPEC projects operating deficits for the State budget to average nearly $145.0 million annually through FY 2010.




This is of particular concern because the State is projected to rely on fewer income taxpayers to pay for public services. In 2000, there were nearly 40,000 Federal income tax filers in the State that had adjusted gross incomes of $100,000 or more. These taxpayers paid approximately 56.8 percent of the total Federal income tax burden collected in Rhode Island. By 2010, RIPEC projects that there will be nearly 65,000 filers earning $100,000 or more, and their share of income taxes will represent 65.6 percent. While this in part reflects changes in relative wealth, it also shows that it is incumbent on policymakers to ensure that the income tax burden remains competitive so that these taxpayers remain in the State.

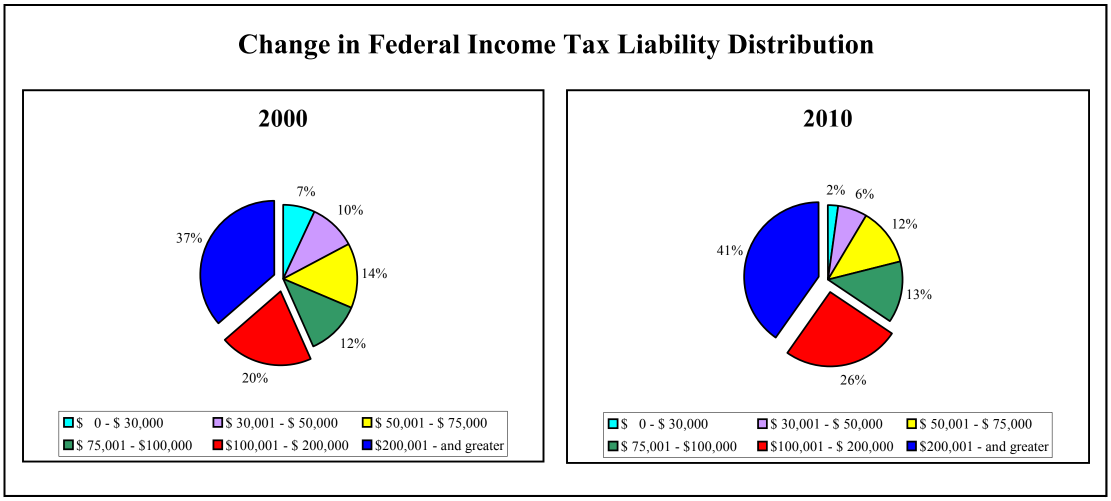
The personal income tax introduces progressivity into a state's tax system, thus helping to reduce the generally regressive nature of other state and local taxes. However, if the income tax structure is not competitive with neighboring and competitor states, it could have an impact on economic development and future tax revenues the State will need to support educational, infrastructure and health and human services functions.

Anecdotal evidence gathered by the Rhode Island Society of CPA's through a survey of their membership indicates that Rhode Island's relatively high marginal tax rate may have an impact on wealth creation and retention in the Ocean State.

Their survey found cases where:

- Retirees were moving to lower tax states;
- Some companies were locating in low tax states and serving the Rhode Island market without establishing taxable nexus; and
- Companies with multiple locations were moving into Rhode Island, but locating higher income wage earners elsewhere[i].

Should the income tax structure discourage upper middle class taxpayers to remain or locate in the Ocean State, there may be a significant impact on the State. The loss of a small number of these taxpayers could have implications for the economy as well as overall state and local revenue product.




To illustrate the potential impact these taxpayers have on the State's income tax revenue, assume that in FY 2010, these 65,000 filers represent approximately $820.0 million (65.6 percent) of the projected $1,251.3 million in State income tax collections. This represents an average income tax burden for these taxpayers of $12,615. If the State were to experience a net loss of 5.0 percent of these filers, this would represent a decline of 3,250 filers. Note that 3,250 filers would represent less than 1.0 percent of the total number of filers projected in 2010. With an average income tax liability of $12,615, this translates into a loss of $41.0 million in FY 2010. This would represent approximately 3.3 percent of projected personal income tax collections in FY 2010.

**Can We Field a Highly Skilled Workforce?**

One disconcerting trend is the projected decline in populations projected in key age cohorts for Rhode Island. The 35-49 population is projected to decline by 7.5 percent, from 245,739 in 2000 to a projected 227,424 in 2010. As a percent of the total population, the 35-49 year old population would decline from 23.4 percent in 2000 to 20.4 percent in 2010.

In addition, public school enrollments are projected to decline for the remainder of the decade. RIPEC has also shown that one in five of the State's workforce in 2020 will come from the State's urban core school systems (Central Falls, Newport, Pawtucket, Providence and Woonsocket).[ii]

These trends raise a number of yellow flags concerning the State's workforce potential, its readiness to compete with neighboring States for good jobs and good wages, and the ability of the State's public school system to adequately prepare our future workforce. Clearly the heart of the economy for the State is a skilled or highly educated workforce that can constantly innovate and meet the increasingly fluid economic demands of the coming decades. If the State's skilled workforce does not show potential for growth, it becomes a barrier for future investment.

In addition to a potentially declining pool of workers and issues of workforce readiness, there is another factor that is beginning to impact the State's workforce – the price of housing. RIPEC and Bank of America released a report on the impact housing has on the State's competitiveness in 2004. The analysis concluded that affordable workforce housing in Rhode Island was essential in establishing a business environment that is competitive and attractive. The major themes that emerged from the research included:

- There is a significant supply/demand imbalance in Rhode Island's housing market;
- Land economics are a contributing factor to low supply and high costs; and
- Rhode Island's housing environment will have a slow, steady negative impact on Rhode Island's business community, particularly as a major pressure on wages.

These findings have recently been confirmed by the Joint Center for Housing Studies of Harvard University. The Center concluded in its *State of the Nation's Housing 2005* report that "natural and regulatory constraints on development have likely contributed to house price gains in areas that have seen the most outsized increases in the past five years. Development constraints drive up land and construction costs as well as prevent new housing from keeping pace with rising demand."[iii]

The current characteristics of the Rhode Island housing market make it increasingly difficult for middle income earners to find adequate housing. The median price of a single family home in the State has increased from approximately $136,000 in 2000 to $264,700 in FY 2004 (based on most recent data available from the Rhode Island Association of Realtors). Over the past five years, the median housing price has experienced an average annual rate of growth of 14.3 percent.

If housing prices in the Ocean State grew at an average annual rate of 6.0 percent for the remainder of the decade, the estimated median price would be approximately $386,000 by 2010. The State's median price would experience an average annual growth rate of 11.0 percent over the decade. Note that personal income growth during the forecast period is projected at 4.0 percent annually. Given the limited supply and the rapid growth in price, the existing Rhode Island housing market is potentially out of reach for most of the State's workforce.

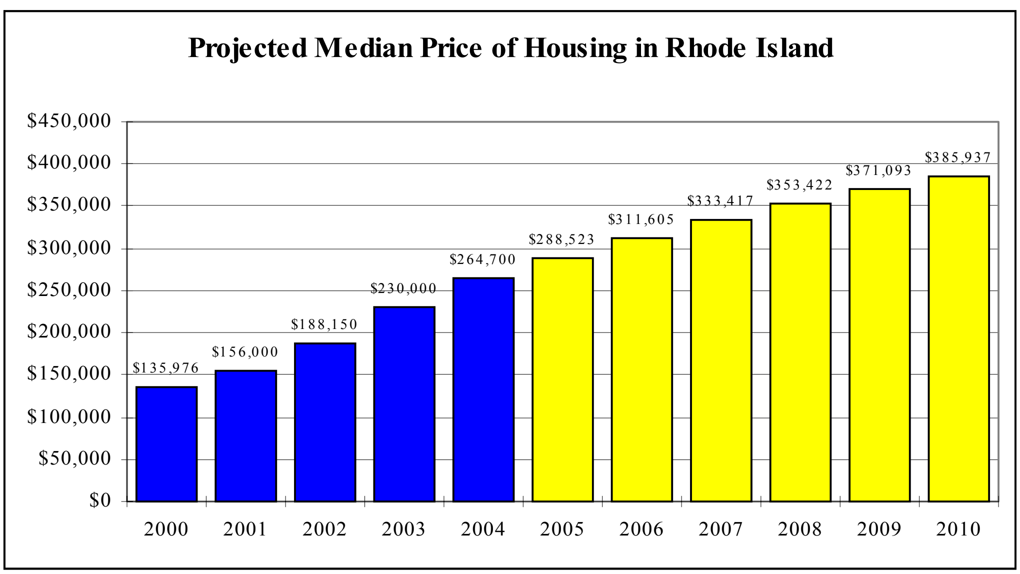


**Table 1**
**State Share of Projected Education Expenditures**

| Fiscal Year | Total Spending* | Change | Percent Change | State Aid** | Change | Percent Change | State Share |
|---|---|---|---|---|---|---|---|
| 2000 | $1,411.6 | $114.5 | 8.8% | $556.0 | $45.6 | 8.9% | 39.4% |
| 2001 | 1,507.2 | 95.6 | 6.8% | 602.3 | 46.3 | 8.3% | 40.0% |
| 2002 | 1,586.3 | 79.1 | 5.2% | 634.0 | 31.7 | 5.3% | 40.0% |
| 2003 | 1,697.3 | 111.0 | 7.0% | 661.8 | 27.8 | 4.4% | 39.0% |
| 2004 | 1,807.1 | 109.8 | 6.5% | 686.5 | 24.7 | 3.7% | 38.0% |
| 2005 | *1,913.4* | *106.3* | *5.9%* | 692.3 | 5.8 | 0.8% | 36.2% |
| 2006 | *2,018.0* | *104.6* | *5.5%* | 716.2 | 23.9 | 3.5% | 35.5% |
| 2007 | *2,131.0* | *113.0* | *5.6%* | *751.7* | *35.5* | *5.0%* | *35.3%* |
| 2008 | *2,241.6* | *110.6* | *5.2%* | *787.7* | *36.0* | *4.8%* | *35.1%* |
| 2009 | *2,345.4* | *103.8* | *4.6%* | *819.4* | *31.7* | *4.0%* | *34.9%* |
| 2010 | *2,444.1* | *98.7* | *4.2%* | *848.5* | *29.1* | *3.6%* | *34.7%* |

*FY 2005 to FY 2010 spending are RIPEC projections. Expenditures include State's contribution to the teacher retirement system, and exclude expenditures relating to State-run schools and charter schools.
**FY 2007 to 2010 State aid are RIPEC projections. State aid includes all aid to school districts except school construction aid and aid to state-operated schools and charter schools.

Source: RI Dept of Education and RIPEC Calculations

**How will school spending demands, high property tax burdens and growing housing prices impact the State's quality of life?**

RIPEC projects that public school enrollment will decline by 2.5 percent from 2000 to 2010 – about 3,800 students. RIPEC projects this decline despite modest increases in school aged children during this period. The declining enrollment is partially attributable to the change in the Kindergarten entrance age. It also may be in part due to increased interest in private and charter schools. However, RIPEC projects public school spending to total more than $2.4 billion by the close of the decade, representing an average annual rate of growth of 4.9 percent for the remainder of the decade. The continued demands placed on the public school systems despite declining enrollments are somewhat perplexing. The State's enrollment is projected to retract somewhat by the end of the decade, but the rate of growth in spending is expected to increase.

Possible reasons could be the continued demand for special education. Special education costs continue to represent the fastest growing program component of the school budget, consuming a greater portion of the total budget. Special education populations are projected to increase from 19.8 percent in 2000 to 21.2 percent in 2010. In addition, baby-boomer aged teachers reaching retirement age combined with overall pension and health care costs continue to be central to the growth in school spending.

A direct impact of these trends can be felt by the property taxpayer in the Ocean State. The property tax in Rhode Island is increasingly relied upon to shoulder a greater portion of the public school burden. While total State education aid (direct aid and teacher retirement) is projected to grow by 4.3 percent annually through the remainder of the decade, it will provide 29.7 percent ($292.5 million) of the net growth in resources available for schools during the 10-year period. RIPEC forecasts that property taxes will have provided $691.9 million, or 70.3 percent of the additional resources to support schools over this period of time. RIPEC projects that the State share of school funding will decrease from 39.4 percent in FY 2000 to 34.7 percent by 2010.

This blend of issues – school spending growth, property tax burdens and limited housing supply – will have an impact on the quality of life in Rhode Island's neighborhoods. Local planning, zoning and marketing strategies may evolve into programs that are more directly linked to how they impact the property tax than the efficient and effective use of limited space. In addition, given the declining population in the age cohorts considered to be in peak earning years as well as a growing elderly population (boomers hit age 65 beginning in 2011), there may be fewer property taxpayers that can afford to shoulder such a burden. Again this returns to the ability of the State to provide the tools and policies necessary to field a workforce that can attract and retain private investment.

**Next Steps – Which Path Will We Take?**

The State's budget policies may need to be enhanced to adequately handle future challenges given budget drivers and State's demographic trends. As noted above, the baby boomers are beginning to show up in the elderly bubble in 2011 and will reach 21.4 percent of total population by 2030. Public employer pension contributions are projected to grow by 50.0 percent over next five years, requiring $125.0 million in additional funds through FY 2010, and public school spending is projected to grow at twice the rate of inflation despite projected enrollment declines. Couple these demographic trends with Medicaid expenditures projected to annually grow by 8.2 percent and consuming 30.0 percent of the State's general revenue budget by 2010, it is clear that the State will need to prepare itself for difficult financial choices.

One possibility is to muddle through the problems each year, annually patching up state and local budgets. This path focuses on near term solutions, incrementally adjusting policies to fit the immediate need and using creative revenue streams to balance the books. However, the first path has its consequences. The State would continue to experience "moderate" budget deficits (3-4 percent), and spending would continue to be determined by available resources. The State would not be prepared for potential Federal changes to the Medicaid program, and entitlement spending (primarily Medicaid) will continue to limit Rhode Island's ability to reduce taxes or make investments, while fewer taxpayers shoulder more of the income tax burden. Localities will continue to experience escalating property taxes and diffuse development patterns, primarily driven by school spending despite declining enrollments statewide.

The second path will take considerable political will, courage and determination. Taking this path could lead to State and local governments providing high quality, affordable, public services for the citizens of Rhode Island. Achieving this goal will require addressing the projected operating deficits and basing budget decisions on buying results for Rhode Island taxpayers, and using finite public resources to add value by enhancing economic opportunities. Achieving this end will require new tools and informed public input to help decision-makers focus on choices, cost and benefits, and tax competitiveness.

Choosing this path should not be seen as just countering pressure from the various budget drivers and demographic trends outlined in *Rhode Island 2010*, but as a direction that fosters strategic thinking and bring reforms that will enable governments produce better outcomes for less money.

The path to Rhode Island's future requires that transformational change are made in the way State and local governments operate and make budget choices in order to:

- Deliver essential public services at a price Rhode Islanders can afford and are willing to support; and
- Focus public spending decisions on adding value and buying results rather than cutting or adding to last year's spending levels.

Transformational practices and procedures should be built into the budgeting process to address the structural budget deficit, provide adequate resources needed to fund spending that is driven by demographic change, and make investments to grow the State economy.

*Tax and Spending Limitation*

One key transformational change could be the adoption of a constitutional limit on State and local spending. Since the late 1970s, over half of the states (including Rhode Island) have enacted either a constitutional or statutory TEL. A TEL is a provision in state law that restricts the growth in either revenue or spending at both the state and/or local levels. Research on the effectiveness of TELs has been mixed. Analysis indicates that the effectiveness of TELs is influenced by how well TELs are designed. Effective TELs limit spending growth, are constitutional, apply to both state and local government, and refund excess revenues directly to taxpayers.

Decision-makers should address the following questions. Would adoption of a TEL:

- Enhance fiscal discipline and affordable government?
- Improve tax competitiveness thus encouraging job creation and economic development?
- Counter pressure from demographic trends for more spending that does consider services citizens value most?

The discussion of a TEL should be viewed as an opportunity to help make government more affordable, efficient, and effective as well as responsive to the needs of citizens. If enacted, it will be critical to ensure State and local governments are prepared to live within a TEL. This will require understanding how much citizens are willing to spend on fundamental services, what results citizens expect from public programs, and how best to allocate limited funds to achieve these core goals.

Given the demands entitlement programs are placing on budget choices, RIPEC urges the Governor to create a joint public-private affordability task force. The first undertaking of such a task force could be entitlement reforms.

*Entitlement Reform*

Social service programs that provide direct assistance are projected to consume nearly \$0.45 of every new \$1.00 spent between FY 2006 and FY 2010. These programs are mainly driven by five variables – demographic trends, economic circumstances of the State's population, the policies that establish the scope of services, the thresholds for eligibility for the services in the State, and medical inflation.

The largest program is clearly Medicaid, which is projected to increase its share of total general revenue spending from 22.4 percent in FY 2000 to a projected 30.0 percent in FY 2010. RIPEC forecasts Medicaid spending to increase at an average annual rate of 8.2 percent from FY 2006 through FY 2010. Medicaid alone will represent nearly 41.0 percent of the net growth in spending from FY 2006 to FY 2010 - $310.3 million of the $765.6 million in projected general revenue growth. By FY 2010, RIPEC projects that one in five Rhode Islanders will participate in Medicaid programs.

To further illustrate the impact different demographic trends can have on State spending, consider the following. RIPEC projects that the number of child care slots will increase by 18.9 percent from FY 2006 though FY 2010. RIPEC projects that every 1.0 percent increase in child care slots requires an additional $0.4 million appropriation in general revenues. Conversely, RIPEC projects the caseload for elderly receiving Medicaid services to increase by 8.9 percent during this forecast period. RIPEC projects that every 1.0 percent increase in the elderly caseload will require $2.5 million in additional general revenues.

The State's political and business leadership need to demonstrate the political will to begin addressing the fastest growing component of the State budget – Medicaid. It is not a question of necessarily reducing entitlements. Rather, it is about designing a social service system that maximizes taxpayers' dollars and controlling the rate of growth in spending through cost effective and efficient service delivery.

## IV. Demographic Patterns

**Summary**

Population Growth

- Rhode Island's population is projected to increase by 6.5 percent - from 1,048,319 in 2000 to 1,116,652 in 2010 – compared to projected 9.8 percent Nationally;
- Almost two-thirds of the growth in population between 2000 and 2010 will occur in Providence County, accounting for almost 60.0 percent of the total population in 2010;
- Bristol County is projected to be the fastest growing county, increasing by 9.3 percent between 2000 and 2010; and
- Newport County is projected to experience the only decline among the counties, declining by 2.8 percent.

Population Growth by Subgroups

- The major shift in age cohorts between 2000 and 2010 will be among the 50-64 year old population, which is projected to increase by 38.6 percent, to 215,470 in 2010. As a percent of the total population, this age cohort is projected to account for almost one-fifth of the population in 2010, up from 14.8 percent in 2000;
- Conversely, the 35-49 year old population will decline by 7.5 percent to a projected 227,424 in 2010, accounting for 20.4 percent of the population in 2010, declining from 23.4 percent in 2000;
- While the number of school-aged children (ages 5-17) is projected to increase by 4.9 percent between 2000 and 2010, Rhode Island's public school enrollment (excluding charter and state-run schools) is projected to decline by 2.5 percent, from 155,351 in 2000 to 151,535 in 2010;
- RIPEC projects the number of children receiving special education services to represent 21.2 percent (32,071 pupils) of total enrollment statewide by 2010, up from 19.8 percent in 2000 (30,704 students);
- The baby-boomer generation will begin moving into the 65 years of age and above by the close of the decade (2011). This age group is projected to account for 14.5 percent by 2010 and for 21.4 percent of the total population by 2030;
- The pool of Medicaid eligible Rhode Islanders will continue to grow through the balance of the decade, increasing to about 281,000 by 2010, representing one-quarter of the population by 2010;
- About one-fifth of the State's population is projected to participate in Medicaid in 2010, up from 14.0 percent in 2000;
- The Family Independence Program caseload is projected to decline by nearly 45.0 percent (23,000 people) between 2000 and 2010 to 28,504; and
- During the same time period, State-subsidized child care slots increased by 44.3 percent (4,677 slots) to 15,230.

*National Population Patterns* - The demographic factors in this section are based on data from the United States Census. The most recent population forecasting by the Census was completed in April 2005. Nationally, the population increased by 13.2 percent from 1990 to 2000, increasing from 248.7 million to 281.4 million people. The United States Census forecast shows that the Nation's total population will grow to 308.9 million by 2010, representing an increase of 9.8 percent over the decade.

The Census divides the Nation into four regions, Northeast, Midwest, South, and West. The West is projected to experience the largest projected population increase between 2000 and 2010, increasing by 14.2 percent. The second fastest growing region is the South, projected to increase by 13.3 percent during that time period. The Midwest is projected to increase its population by 4.7 percent. As a percent of the total population, the Midwest will decline from 22.9 percent in 2000 to 21.8 percent in 2010.

The Northeast is projected to have the lowest increase of all regions, increasing by 4.1 percent between 2000 and 2010. The Northeast encompasses the New England states, as well as New York, New Jersey and Pennsylvania. As a percent of the total population, the Northeast is projected to lose about 1.0 percentage point between 2000 and 2010, declining from 19.0 percent of the total population in 2000 to 18.1 percent in 2010. Within the Northeast, population increases range from a high of 12.1 percent in New Hampshire to a low of 2.5 percent in Pennsylvania and New York.

**Table 2**
**Population Projections for the United States**

| | 2000 | | 2010 | | Change 2000-10 | |
|---|---|---|---|---|---|---|
| Region | Total | % of Total | Total | % of Total | Amount | Percent |
| United States | 281,421,906 | | 308,935,581 | | 27,513,675 | 9.8% |
| Northeast (1) | 53,594,378 | 19.0% | 55,785,179 | 18.1% | 2,190,801 | 4.1% |
| New England | 13,922,517 | 4.9% | 14,738,789 | 4.8% | 816,272 | 5.9% |
| Maine | 1,274,923 | 0.5% | 1,357,134 | 0.4% | 82,211 | 6.4% |
| New Hampshire | 1,235,786 | 0.4% | 1,385,560 | 0.4% | 149,774 | 12.1% |
| Vermont | 608,827 | 0.2% | 652,512 | 0.2% | 43,685 | 7.2% |
| Massachusetts | 6,349,097 | 2.3% | 6,649,441 | 2.2% | 300,344 | 4.7% |
| **Rhode Island** | **1,048,319** | **0.4%** | **1,116,652** | **0.4%** | **68,333** | **6.5%** |
| Connecticut | 3,405,565 | 1.2% | 3,577,490 | 1.2% | 171,925 | 5.0% |
| Midwest (2) | 64,392,776 | 22.9% | 67,391,433 | 21.8% | 2,998,657 | 4.7% |
| South (3) | 100,236,820 | 35.6% | 113,583,614 | 36.8% | 13,346,794 | 13.3% |
| West (4) | 63,197,932 | 22.5% | 72,175,355 | 23.4% | 8,977,423 | 14.2% |

(1) Northeast: Includes New England States, New York, New Jersey, Pennsylvania
(2) Midwest: Includes Ohio, Indiana, Illinois, Michigan, Wisconsin, Minnesota, Iowa, Missouri, North Dakoka, South Dakota, Nebraska, Kansas
(3) South: Includes Delaware, Maryland, DC, Virginia, West Viginia, North Carolina, South Carolina, Georgia, Florida, Kentucky, Tennessee, Alabama, Mississippi, Arkansas, Louisina, Oklahoma, Texas
(4) West: Includes Montana, Idaho, Wyoming, Colorado, New Mexico, Arizona, Utah, Nevada, Washington, Oregon, California, Aslaka, Hawaii

Source: U.S. Census, Interim Projections for the States, April 21, 2005, and RIPEC calculations.

## Table 3
**Rhode Island Population By County**

| Counties (1) | 2000 Total | 2000 Share | 2010 Total | 2010 Share | Change 2000-10 Percent | Change 2000-10 Amount |
|---|---|---|---|---|---|---|
| Providence County | 621,602 | 59.3% | 665,680 | 59.6% | 7.1% | 44,078 |
| Kent County | 167,090 | 15.9% | 178,451 | 16.0% | 6.8% | 11,361 |
| Washington County | 123,546 | 11.8% | 134,131 | 12.0% | 8.6% | 10,585 |
| Newport County | 85,433 | 8.1% | 83,028 | 7.4% | -2.8% | (2,405) |
| Bristol County | 50,648 | 4.8% | 55,362 | 5.0% | 9.3% | 4,714 |
| **Total** | **1,048,319** | | **1,116,652** | | **6.5%** | **68,333** |

Providence County: Burrillville, Central Falls, Cranston, Cumberland, East Providence, Foster, Glocester, Johnston, Lincoln, North Providence, North Smithfield, Pawtucket, Providence, Scituate, Smithfield and Wonnsocket
Kent County: Coventry, East Greenwich, Warwick, West Greenwich and West Warwick
Washington County: Charlestown, Exeter, Hopkinton, Narragansett, New Shoreham, North Kingstown, Richmond, South Kingstown and Westerly
Newport County: Jamestown, Little Compton, Middletown, Newport, Porstmouth and Tiverton
Bristol County: Barrington, Bristol and Warren.

Source: U.S. Census, and RIPEC calculations for 2010.

*Rhode Island's Growth Patterns* - Rhode Island's population is projected to increase by 6.5 percent between 2000 and 2010, increasing to 1,116,652 in 2010. However, there are different rates of growth in population by county, which in turn results in different types of pressure on housing, land use and public services. The Census does not project population by county. Therefore, RIPEC used the latest Census estimate for counties for 2004 and projected population by county until 2010. Based on this projection, nearly two-thirds of the growth in population will occur in Providence County. This will increase the population for this county by 44,078 people, from 621,602 in 2000 to a projected 665,680 in 2010. Providence County is projected to account for 60.0 percent of the State's total population in 2010, about the same percentage as in 2000.

Bristol County is projected to experience the highest growth rate, increasing by 9.3 percent, from 50,648 people in 2000 to 55,362 in 2010. This will slightly increase the share of the total State population from 4.8 percent in 2000 to 5.0 percent in 2010. Washington County is projected to have the second highest growth rate, increasing its population by 8.6 percent, from 123,546 in 2000 to 134,131 in 2010. Newport County is projected to experience the only decline among the State's counties. Its population is projected to decline by 2.8 percent (2,405 people) from 85,433 in 2000 to 83,028 in 2010.

*Population by Age* - Table 4 shows the major shift in age cohorts between 2000 and 2010 will be among the 50-64 year old population which is projected to increase by 38.6 percent, from 155,423 in 2000 to 215,470 in 2010. As a percent of the total population, this age cohort is projected to account for almost one-fifth of the population in 2010, up from 14.8 percent in 2000. Conversely, the 35-49 population will decline by 7.5 percent, from 245,739 in 2000 to a projected 227,424 in 2010. As a percent of the total population, the 35-49 year old population will decline from 23.4 percent in 2000 to 20.4 percent in 2010. These projections may have implications

**Table 4**
**Rhode Island Population by Age Cohort**

| Age | 2000 Amount | 2000 Share | 2010 Amount | 2010 Share | Change 2000-10 Amount | Change 2000-10 Percent |
|---|---|---|---|---|---|---|
| 0-4 | 63,896 | 6.1% | 66,193 | 5.9% | 2,297 | 3.6% |
| 5-19 | 218,720 | 20.9% | 220,178 | 19.7% | 1,458 | 0.7% |
| 20-34 | 212,139 | 20.2% | 230,029 | 20.6% | 17,890 | 8.4% |
| 35-49 | 245,739 | 23.4% | 227,424 | 20.4% | (18,315) | -7.5% |
| 50-64 | 155,423 | 14.8% | 215,470 | 19.3% | 60,047 | 38.6% |
| 65-85+ | 152,402 | 14.5% | 157,358 | 14.1% | 4,956 | 3.3% |
| **Total** | **1,048,319** | | **1,116,652** | | **68,333** | **6.5%** |

Source: U.S.Census Bureau, Population Division, Interim State Population Projections, as of April 21, 2005 and RIPEC calculations.

for the state of Rhode Island's workforce that will be available by the end of the decade.

By the close of the decade, Rhode Island is not projected to see any major shifts in the 5-19 population, where this age cohort is projected to see a slight increase of 0.7 percent between 2000 and 2010. Ages 5-19 represented 20.9 percent of the population in 2000. This is expected to decline to 19.7 percent by the close of the decade.

<u>*Public School Enrollment Forecast*</u> - RIPEC forecasted public K-12 enrollment, as well as eligibility for subsidized lunch programs and children receiving special education services based on regression models. One should note that enrollment numbers do not include enrollment in state-run and charter schools. Fall enrollment in Rhode Island is projected to decline by 2.5 percent, from 155,351 in 2000 to 151,535 in 2010. As long as elementary and secondary education remains compulsory, school-aged population and enrollment should closely mirror each other. The Census projects that school-aged children (aged 5-17 years) will increase on average annually by 0.5 percent between 2000 and 2010 in Rhode Island. However, Rhode Island's public school enrollment is projected to decline annually by 0.2 percent during the same time period.

Reasons for the declining enrollment could include an increased enrollment in private, state-run and charter schools. Enrollment for these schools is not included in RIPEC's forecast. Enrollment in charter schools has increased on average annually by 54.5 percent between 2002 and 2005, and enrollment in state-run schools by 5.6 percent annually between 2000 and 2005. Enrollment in public schools (excluding charter and state-run schools) has declined annually by 0.2 percent during the same time period.

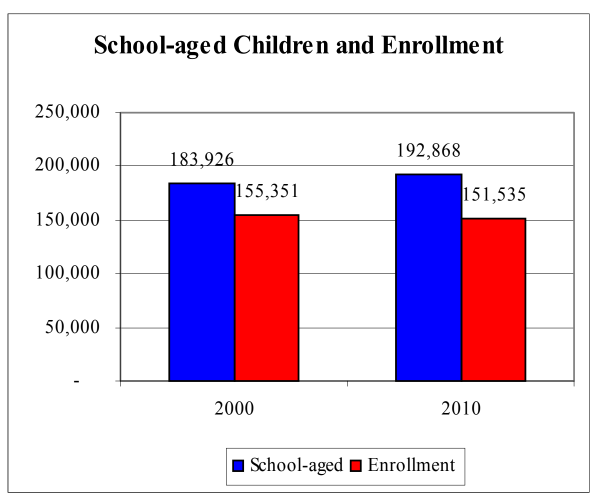


**Table 5**
**Rhode Island Student Demographics**

| Year | Total Enrollment | Subsidized Lunch | Percent Lunch | Special Education | Percent Special |
|---|---|---|---|---|---|
| 1990 | 135,035 | 27,933 | 20.7% | 21,025 | 15.6% |
| 1995 | 146,604 | 47,963 | 32.7% | 25,144 | 17.2% |
| 2000 | 155,351 | 52,787 | 34.0% | 30,704 | 19.8% |
| 2005 | 153,596 | 53,025 | 34.5% | 30,839 | 20.1% |
| *2010** | *151,535* | *53,155* | *35.1%* | *32,071* | *21.2%* |

*2010 are RIPEC projections.
Source: RI Department of Education and RIPEC calculations

RIPEC has projected the number of students that are eligible for subsidized lunch programs and special education services. Children with modest economic backgrounds often require additional services to provide a meaningful educational experience. Concentrations of children with economic disadvantages can also impact the cost of delivering services. Similarly, those receiving special education services require additional resources to meet educational needs. Special education programs represent the fastest growing component of the public education budget, now representing 20.0 percent of school districts' operating budgets.

RIPEC projects the number of children eligible for subsidized lunch programs to total 53,155 by 2010, up slightly (0.7 percent) from 52,787 in 2000. In 2000, the number of children eligible for subsidized lunch programs represented 34.0 percent of total enrollment. RIPEC projects this to increase to 35.1 percent by the end of the decade.

RIPEC projects the number of children receiving special education services to total 32,071 by 2010, up 4.5 percent from 30,704 in 2000. This growth is projected despite overall declines in total enrollment in the State. Therefore, in 2000, the number of children receiving special education programs represented 19.8 percent of total enrollment. RIPEC projects this to increase to 21.2 percent by the end of the decade.

*Elderly Population* - Baby-boomers represent those born between the years 1946-1964. This group of individuals will begin moving into the 65 years of age range and above by the close of the decade (2011). In 2010, the Census projects those of age 65 or older to represent 14.1 percent of the population, slightly lower than in 2000, when this age cohort accounted for 14.5 percent of the population. This age group is projected to increase to 17.2 percent of the total population by 2020 and to 21.4 percent by 2030. However, Rhode Island's ranking within the Nation is projected to drop from 6$^{th}$ highest in 2000 to 15$^{th}$ highest in 2010 and 18$^{th}$ highest by 2030. This shows that the Ocean State is not alone in the aging of its population. Nationally, the people aged 65 and older as a percentage of the total population is projected to grow from 13.0 percent in 2010 to 19.7 percent by 2030. Florida has the highest number of this population, with 17.6 percent of this population being 65 or older in 2000 and a projected 27.1 percent by 2030.

This demonstrates the influence the baby-boomer generation will continue to have on major public policy decisions through 2030. For example, increasing pressure from an aging population will impact programs and services such as long-term care and pharmaceutical assistance programs. The recent SHAPE Study forecasted that by 2010, 550 additional nursing home beds will be needed, assuming the current occupancy rate of 90 percent. According to the SHAPE study, the greatest shortfall will appear after 2020, reflecting the increased number of elderly population. In the study, it is projected that by 2030 Rhode Island will face a gap of 2,400 nursing home beds.[iv]

*<u>Medicaid Eligibles and Recipients</u>* - In 2000, 182,149 Rhode Islander's were eligible for Medicaid services, representing 17.3 percent of the State's total population. In its FY 2006 Medicaid report, RIPEC forecasts that the pool of eligible Rhode Islanders will continue to grow through the balance of the decade, increasing to approximately 281,000 by 2010. These Rhode Islanders would represent approximately one-fourth of the State's total projected population in 2010. This projected growth rate of 54.3 percent over the ten-year period exceeds the overall growth in the State's total population, projected at 6.5 percent during the same period.

The caseload for those actually participating in Medicaid (recipients) is projected to increase from 146,439 in 2000 to 216,950 by 2010 - an increase of 48.2 percent (70,511 people). Overall, about one-fifth of the State's population is projected to participate in Medicaid in 2010, up from 14.0 percent in 2000. However, the projected participation rate is forecast to decline, falling from 80.4 percent in 2000 to 77.2 percent in 2010. This indicates that enrollment in the various Medicaid programs will not keep up with the potential demand from Rhode Islanders who could be eligible for the services.

Because of the rapid growth in children and family beneficiaries, there has been a slight shift in the makeup of the total caseloads. Of the projected 70,511 person increase between 2000 and 2010, nearly 80.0 percent of the growth is projected to occur in children and family

**Table 6**
**Rhode Island Medicaid Caseload**
**FY 2000 to FY 2010**

| | FY 2000 | | FY 2010* | | 2000-2010 Change | |
|---|---|---|---|---|---|---|
| **Population** | **Number** | **Share** | **Number** | **Share** | **Number** | **Percent** |
| Adults with Disabilities | 20,646 | 14.1% | 31,135 | 14.4% | 10,489 | 50.8% |
| Elderly | 18,251 | 12.5% | 22,072 | 10.2% | 3,821 | 20.9% |
| Children & Families** | 107,542 | 73.4% | 163,743 | 75.5% | 56,201 | 52.3% |
| **Total** | **146,439** | | **216,950** | | **70,511** | **48.2%** |

*Caseload for FY 2010 is projected by RIPEC.
** Includes Children & Families in Managed Care and fee-for-service, children with special health care needs and children in foster care.

Source: Department of Human Services and RIPEC calculations.

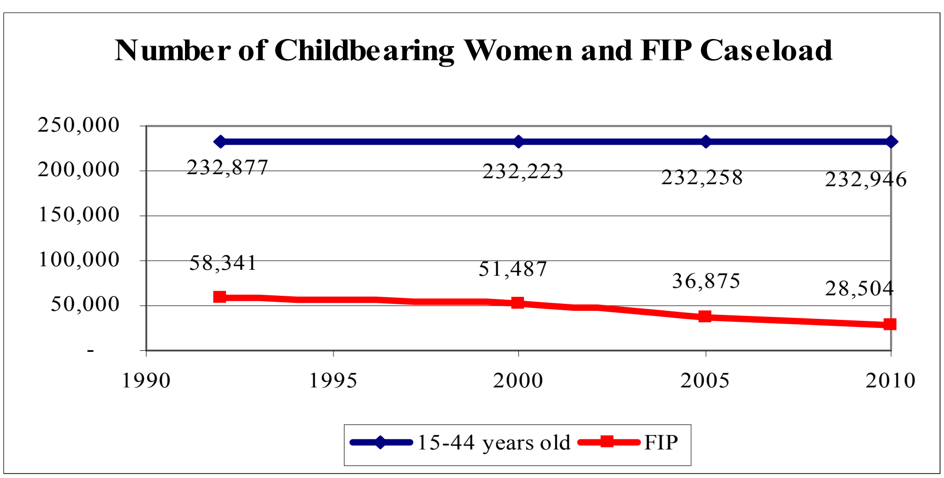
caseloads. Children and families accounted for 73.4 percent of the total caseload in 2000 and are projected to increase to 75.5 percent in 2010. The caseload will increase from 107,542 in 2000 to a projected 163,743 in 2010, increasing by 52.3 percent.

In 2010, the share of adults with disabilities as a percentage of the total Medicaid caseload will remain essentially unchanged at 14.4 percent. RIPEC projects that the enrollment will increase from 20,646 in 2000 to 31,135 in 2010, increasing by 50.8 percent (10,489 persons). The caseload for the elderly increased from 18,251 in 2000 to a projected 22,072, increasing by 20.9 percent (3,821 persons). As a percent of the total caseload, the elderly declined from 12.5 percent of the total caseload in 2000 to a projected 10.2 percent in 2010. However, one should note that the baby boomers will not affect the elderly caseload until 2011, beyond RIPEC's forecasted period.

*Family Independence Program* - The Family Independence Program (FIP) is Rhode Island's welfare program providing cash assistance, as well as education, training and employment services to low income working parents and those preparing for work.

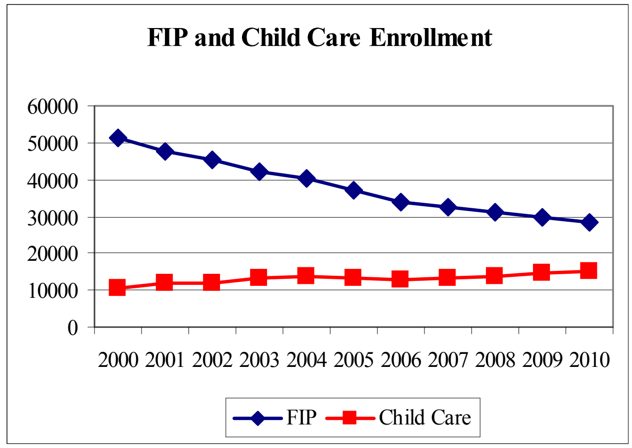
RIPEC has looked at the relationship between the number of childbearing women (15-44 years age range) and the TANF/FIP caseload in Rhode Island. Females between the ages of 15 and 44 decreased slightly by 0.3 percent during the 1990s while the TANF/FIP caseloads declined by 12.0 percent during that time period. However, between 2000 and 2005 the number of FIP caseloads declined while this female age group stayed stagnant. Caseloads declined by 28.4 percent, from 51,487 in 2000 to 36,875 in 2005; but the number of females aged 15 to 44 remained basically unchanged, increasing by an estimated 35 persons during that five-year. The Census forecasts that the 15-44 age group of females will slightly increase to 232,946 in 2010.

The data suggest that the FIP caseload is not so much driven by that age cohort than it is by the impact of the State's welfare reform initiatives as well as overall economic trends. Based on these findings and assuming no changes in current policies, RIPEC projects that – despite a projected increase in the number of childbearing women - the FIP caseload will decline to 28,504 people in 2010. This would translate into a decline of almost 23,000 persons since 2000. or 45.0 percent.



*Child Care Slots* - Increasing child care slots was part of welfare reform to assist low income families stay employed. Child care slots increased from 10,553 slots in 2000 to a peak number of slots of 13,601 in 2004. It has declined in the past two years and is estimated to total 12,804 in 2006.

An important aspect is the demand for State-subsidized child care slots, as measured by the number of children under five. The number of children under five declined by 6.6 percent in the 1990s and by 1.0 percent between 2000 and 2005. The Census projects that the number of children under five years of age will increase by 4.6 percent between 2005 and 2010. When linking the actual number of child care slots and the demand it shows that in 1990 4.5 percent of the children under five received State-subsidized child care slots. This has increased to 16.5 percent in 2000 and 20.7 percent in 2005 - meaning that one-fifth of the children under five received State-subsidized slots in 2005.




Based on a regression model, RIPEC projects that child care slots will increase to 15,230 by 2010. Between 2000 and 2010, child care slots would increase by 44.3 percent or 4,677 slots. Assuming no changes in policies, RIPEC projects that child care slots will increase by 16.4 percent between 2005 and 2010, more than three times as fast as the number of children under five years. This would translate into 23.0 percent of the children under five having a State-subsidized child care slot in 2010.

## Table 7
### Selected Caseload Trends

| Caseload | 2000 | *2010** | Estimated Change | Percent Change |
|---|---|---|---|---|
| Medicaid Recipients | 146,439 | *216,950* | 70,511 | 48.2% |
| FIP/TANF | 51,487 | *28,504* | (22,983) | -44.6% |
| Child Care | 10,553 | *15,230* | 4,677 | 44.3% |

* RIPEC projections

Source: RI DHS and RIPEC calculations.

## V. Selected Measures of Income and Residential Property Wealth

**Summary**

There are many measures of economic activity and income, such as personal income, Median Family Income, disposable income, changes in the housing market, as well as the consumer price index. The following focuses attention on personal income, Median Family Income, and the median price of housing.

Median income can serve as an indicator of relative wealth and income distribution. Comparing median income can be useful in understanding differences and how higher incomes influence relative positions among the states. Total personal income growth can reflect potential trends in overall income wealth in a State, and can serve as a reasonable indicator of future consumer demand. While both measures can provide insight into income trends, they both have limitations. For example, recessions can occur when consumers stop spending, which in turn drives down income growth. One may miss the turning point in an economy (such as when consumers stop spending) if one looks solely at income growth.

A more difficult task is projecting housing market trends. The market is a function of national trends, Federal monetary policy, and regional and local conditions, such as employment, land use and development restrictions and the like. The following highlights some of the findings in this section of the report:

- RIPEC projects Rhode Island's personal income will grow at an average annual rate of 4.0 percent during the forecast period, totaling $46.2 billion by 2010 (Compared to 3.7 Nationally and 3.4 percent in New England);
- Connecticut and Massachusetts' personal income represents 75.0 percent of the total personal income in New England. Rhode Island's personal income represents 6.4 percent of the Region's personal income;
- Rhode Island's Median Family Income is projected to increase from $71,098 in FY 2006 to $79,321 in FY 2010 – representing an average annual growth rate of 2.7 percent;
- Rhode Island's Median Family Income will be 10.1 percent higher than the U.S. Median ($72,013) – compared to 16.2 percent above the U.S. in FY 2000);
- In 2000, there were nearly 40,000 Federal income tax filers in the State that had adjusted gross incomes of $100,000 or more providing 56.8 percent of the total Federal income tax burden collected in Rhode Island;
- By 2010, RIPEC projects that there will be nearly 65,000 filers earning $100,000 or more, and their share of income taxes will represent 65.6 percent;
- Over the past five years, the median housing price of a single family home has experienced an average annual rate of growth of 14.3 percent; and
- RIPEC projects that if the Rhode Island median housing price experiences a 6.0 average annual rate of growth for the remainder of the decade, the median price of a single family home will hit $386,000.

*Personal Income* - According to the Bureau of Economic Analysis (U.S. Department of Commerce), personal income represents all sources of income received by individuals. It includes income received from participation in economic production as well as from government and business transfer payments. It is the sum of compensation, supplements to wages and salaries, and other cash receipts. Clearly the largest component of total income is wages and salaries. Beyond that, there are many other categories of income, including rental income, government subsidy payments, interest income, and dividend income.[v]

Total personal income in the United States increased to $9.7 trillion in 2004 (most recent data available). Since 2000, personal income in the United States has increased at an average annual rate of 3.5 percent. In New England, total personal income has increased to $572.5 billion in 2004, increasing at an average annual rate of 3.2 percent between 2000 and 2004.

Rhode Island's total personal income increased from $30.7 billion in 2000 to $36.5 billion in 2004 - increasing at an average annual rate of 4.4 percent over this period. In 2000, Rhode Island's total personal income represented 6.1 percent of the total personal income in New England. This has since increased slightly to 6.4 percent in 2004.

Among the New England states, the average annual increase in total personal income since 2000 ranged from a low of 2.8 percent in Massachusetts to a high of 5.0 percent in Maine. It should be noted that approximately 75.0 percent of the region's personal income is located in Connecticut and Massachusetts.

*Projected Personal Income* - The following analysis projects total personal income for each of the New England States and the United States as a whole using a simple linear regression model. For comparison purposes, RIPEC has also included an alternative forecast for Rhode Island personal income based on agreed upon projected growth rates established at the Rhode Island Consensus Economic Forecast in May 2005.[vi]

RIPEC projects personal income in Rhode Island will increase to approximately $46.2 billion by FY 2010, representing an average annual rate of growth of 4.0 percent during the forecast period (2005 – 2010). The U.S. average annual rate of growth is projected at 3.7 percent and New England at 3.4 percent during the forecast period.

In May 2005, the Rhode Island Consensus Economic Forecast was developed. The forecast included out-year projections for personal income growth in Rhode Island. The forecast translates into an average annual rate of growth in personal income of 4.2 percent over the forecast period. Personal income would top $47.0 billion by FY 2010 based on this forecast. While the Consensus Forecast is projected to grow at an annual average rate of 4.2 percent, the RIPEC forecast shows an average annual rate of growth of 4.0 percent. When compared to the regression model discussed above, it is not until FY 2008 where the forecasts begin to diverge. By 2010 the Consensus Forecast is 2.0 percent higher than the RIPEC regression model.

**Table 8**
**Projected Personal Income Growth In New England**

| Year | Connecticut | Maine | Massachusetts | New Hampshire | Rhode Island | Vermont | New England |
|---|---|---|---|---|---|---|---|
| 2000 | $141.6 | $33.2 | $240.2 | $41.4 | $30.7 | $16.9 | $504.0 |
| 2001 | 147.4 | 35.1 | 249.1 | 42.6 | 32.5 | 17.7 | 524.4 |
| 2002 | 147.1 | 36.6 | 249.9 | 44.1 | 33.2 | 18.4 | 529.2 |
| 2003 | 149.8 | 38.2 | 253.6 | 45.3 | 34.5 | 19.1 | 540.5 |
| 2004 | 159.1 | 40.3 | 268.2 | 48.1 | 36.5 | 20.4 | 572.5 |
| *2005* | *164.0* | *42.0* | *275.6* | *49.9* | *38.0* | *21.3* | *590.7* |
| *2006* | *170.0* | *43.9* | *284.7* | *51.9* | *39.6* | *22.2* | *612.3* |
| *2007* | *175.9* | *45.7* | *293.8* | *54.0* | *41.2* | *23.2* | *634.0* |
| *2008* | *181.9* | *47.6* | *303.0* | *56.0* | *42.9* | *24.2* | *655.6* |
| *2009* | *187.9* | *49.4* | *312.1* | *58.0* | *44.5* | *25.2* | *677.2* |
| *2010* | *193.9* | *51.3* | *321.3* | *60.1* | *46.2* | *26.2* | *698.9* |
| Average Annual rates of Growth | | | | | | | |
| 2000-2004 | 3.0% | 5.0% | 2.8% | 3.8% | 4.4% | 4.8% | 3.2% |
| 2005-2010 | 3.4% | 4.1% | 3.1% | 3.8% | 4.0% | 4.2% | 3.4% |
| 2000-2010 | 3.2% | 4.5% | 3.0% | 3.8% | 4.2% | 4.5% | 3.3% |

Note: 2000-2004 actual data - 2005 - 2010 RIPEC forecast

Source: RIPEC forecast based on Bureau of Economic Analysis Data (Expressed in Billions)

*Median Family Income* - The following analysis projects Median Family Income (MFI) for four-person families in each of the New England States and the United States as a whole using a simple linear regression model based on data available from CY 1974 through and including CY 2003. If one wishes to report this data in fiscal years (mostly for aid and social service program needs), the United States Bureau of the Census has a three-year lag, in that CY 1974 relates to FY 1977 and CY 2003 relates to FY 2006.

A family is a group of two people or more related by birth, marriage, or adoption and residing together; all such people (including related subfamily members) are considered as members of one family.[vii] The U.S. Bureau of the Census defines Median Income as the amount which divides the income distribution into two equal groups, half having income above that amount, and half having income below that amount.[viii]

Income as used and defined in Median Family Income includes money income received, such as earnings, unemployment and workers compensation, interest and dividends and child support (but is exclusive of certain money receipts, such as capital gains) before payments for personal income taxes, social security, union dues, Medicare deductions, etc.

The Census Bureau does not include the following receipts as income: (1) capital gains from the sale of property, including stocks, bonds, a house, or a car; (2) withdrawals of bank deposits; (3) money borrowed; (4) tax refunds; (5) gifts; and (6) lump-sum inheritances or insurance payments. Income also excludes non-cash benefits, such as food stamps, health benefits, and rent-free housing.[ix]

From 2000 though 2006, the National MFI increased by 22.0 percent, which translates into an average annual rate of growth of 3.4 percent. Rhode Island's MFI increased from $62,005 in FY 2000

**Table 9**

**Projected Median Family Income Growth - 2000-2010**

| Year | United States | Connecticut | Maine | Massachusetts | New Hampshire | Rhode Island | Vermont |
|---|---|---|---|---|---|---|---|
| 2000 | $53,350 | $72,706 | $48,043 | $65,012 | $59,981 | $62,005 | $51,814 |
| 2001 | 56,061 | 74,537 | 50,444 | 68,846 | 60,665 | 62,775 | 53,335 |
| 2002 | 59,981 | 75,505 | 57,536 | 71,689 | 65,885 | 64,614 | 57,713 |
| 2003 | 62,228 | 82,702 | 56,186 | 78,025 | 71,661 | 68,418 | 59,125 |
| 2004 | 63,278 | 82,517 | 58,425 | 80,247 | 72,606 | 70,446 | 62,938 |
| 2005 | 62,732 | 81,891 | 58,802 | 78,312 | 72,369 | 67,646 | 62,331 |
| 2006 | 65,093 | 86,001 | 59,596 | 82,561 | 79,339 | 71,098 | 65,876 |
| *2007* | *66,697* | *88,249* | *62,044* | *83,449* | *76,699* | *73,207* | *65,622* |
| *2008* | *68,469* | *90,721* | *63,769* | *85,801* | *78,858* | *75,245* | *67,451* |
| *2009* | *70,241* | *93,193* | *65,494* | *88,153* | *81,018* | *77,283* | *69,280* |
| *2010* | *72,013* | *95,664* | *67,219* | *90,504* | *83,177* | *79,321* | *71,109* |
| Average Annual Rates of Growth | | | | | | | |
| 2000-2006 | 3.4% | 2.8% | 3.7% | 4.1% | 4.8% | 2.3% | 4.1% |
| 2007-2010 | 2.6% | 2.7% | 2.7% | 2.7% | 2.7% | 2.7% | 2.7% |
| 2000-2010 | 3.0% | 2.8% | 3.4% | 3.4% | 3.3% | 2.5% | 3.2% |

Note: 2000-2006 actual data - 2007 - 2010 RIPEC forecast

Source: RIPEC forecast based on Bureau of Economic Analysis Data (Expressed in Billions)

to $71,098 in FY 2006 – increasing at an average annual rate of 2.3 percent over this period. In FY 2000, Rhode Island's MFI was 16.2 percent above the United States median, whereas it has decreased to 9.2 percent above the United States median in FY 2006. Connecticut, Massachusetts and New Hampshire continue to have higher Median Family Incomes than Rhode Island.

*Projected Median Family Income* - RIPEC projects Rhode Island's Median Family Income (MFI) to increase from $71,098 in 2006 to $79,321 by FY 2010. This will translate into an average annual rate of growth of 2.7 percent during the forecast period. RIPEC projects that the United States median will reach $72,013 by FY 2010, with an average annual rate of growth of 2.6 percent during this period. Therefore, Rhode Island's MFI is projected to be 10.1 percent above the United States median by 2010.

*Income Taxpayer Profiles in Rhode Island* - RIPEC projects a continued shift in how income taxes are generated in the state and a greater dependence on fewer taxpayers to generate income tax revenues to support current programs. As the discussion below will show, over a 10-year period, the top wage earners ($100,000 adjusted gross income or more) will increase their share of total Federal income tax liability in the Ocean State from 56.8 percent in 2000 to 65.6 percent by 2010. In 2000, these taxpayers represented 38.4 percent of the adjusted gross income in the State. This is projected to increase to 43.9 percent by 2010.

As shown on Table 10, in 2000, there were 494,475 Federal income tax returns in Rhode Island. Approximately half (260,561, or 52.7 percent) of the total number of income tax returns was filed with adjusted gross earnings of $30,000 or less. This group of income tax filers represented approximately 14.9 percent of the State's total adjusted gross income and 6.8 percent of the net Federal income tax liability generated in the Ocean State. Conversely, of the 494,475 Federal income tax returns filed in 2000, approximately 8.0 percent were filed by those with adjusted gross income of

**Table 10**
**Rhode Island Income Tax Return Profiles**

| Adjusted Gross Income | 2000 | Share | 2010 | Share |
|---|---|---|---|---|
| *Number of Returns* | | | | |
| $ 0 - $ 30,000 | 260,561 | 52.7% | 220,518 | 42.1% |
| $ 30,001 - $100,000 | 194,454 | 39.3% | 237,851 | 45.4% |
| $100,001 - and greater | 39,460 | 8.0% | 65,184 | 12.5% |
| **Total** | **494,475** | | **523,553** | |
| *Adjusted Gross Income (Millions)* | | | | |
| $ 0 - $ 30,000 | 3,437.5 | 14.9% | 3,036.9 | 10.0% |
| $ 30,001 - $100,000 | 10,749.9 | 46.7% | 14,053.2 | 46.1% |
| $100,001 - and greater | 8,827.7 | 38.4% | 13,364.4 | 43.9% |
| **Total** | **23,015.2** | | **30,454.4** | |
| *Federal Tax Liability(Millions)* | | | | |
| $ 0 - $ 30,000 | 235.1 | 6.8% | 96.7 | 2.3% |
| $ 30,001 - $100,000 | 1,257.1 | 36.4% | 1,349.0 | 32.1% |
| $100,001 - and greater | 1,959.8 | 56.8% | 2,754.0 | 65.6% |
| **Total** | **3,452.0** | | **4,199.7** | |

Source: Statistics of Income, various years and RIPEC forecast

$100,000 or more. These 39,460 returns represented 38.4 percent of the State's total adjusted gross income, and 56.8 percent of the total Federal income tax liability levied in Rhode Island.

From 2000 to 2010, RIPEC projects a 5.9 percent increase in the total number of Federal income tax filers – approximately 29,100 additional net filers. The number of filers for those earning $30,000 or less is projected to decline by 15.4 percent – from 260,600 in 2000 to 220,500 in 2010, while those earning $100,000 or more increased by 65.2 percent – from 39,500 in 2000 to 65,300 in 2010.

From 2000 to 2010, there is a 32.3 percent increase projected in the adjusted gross income from which income taxes would be based. The adjusted gross income for filers earning $30,000 or less is projected to decline by 11.7 percent – from $3.4 billion in 2000 to $3.0 billion in 2010, while those earning $100,000 or more would increase by 51.2 percent – from $8.8 billion in 2000 to $13.4 billion in 2010.

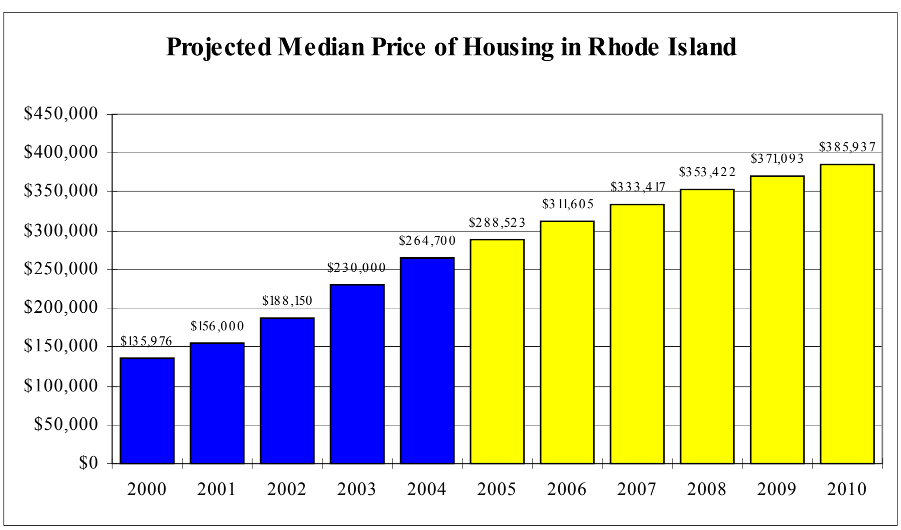
From 2000 to 2010, there is a 21.7 percent increase projected in the total Federal income tax liability in the State – from $3.5 billion to $4.2 billion in 2010. Filers earning $30,000 or less are projected to have a 58.9 percent decline in total Federal income tax liability over this period - from $235.1 million in 2000 to $96.7 million in 2010, while those earning $100,000 or more increased by 40.5 percent – from $1,959.8 million in 2000 to $2,754.0 million in 2010.

Therefore, by the end of the decade, RIPEC projects that the number of returns in Rhode Island will total 523,600, with approximately 42.1 percent of the returns submitted by earners of $30,000 or less. This group of income tax filers are projected to represent approximately 10.0 percent of the State's total adjusted gross income and 2.3 percent of the net Federal income tax liability generated in the Ocean State. Conversely, of the 523,600 Federal income tax returns projected to be filed in 2010, approximately 12.4 percent are projected to be filed by those with adjusted gross income of $100,000 or more. These 65,300 returns would represent 43.9 percent of the State's total adjusted gross income, and 65.6 percent of the total Federal income tax liability levied in Rhode Island.

*Housing Prices in Rhode Island* - Another measure of changing wealth over time is the price of housing in the State. Americans have much of their wealth invested in their homes, and Rhode Island has been experiencing significant growth in its residential housing market. The price of housing affects location decisions within and around the State as well as the local wealth of the community. A recent study developed by RIPEC and Bank of America concluded that affordable workforce housing in Rhode Island was essential in establishing a business environment that is competitive and attractive, and that the scarcity of developable land and a highly regulated market were contributing to the limited supply of housing and therefore translating into significant price valuation. According to the Joint Center for Housing Studies of Harvard University, development constraints drive up land and construction costs as well as prevent new housing from keeping pace with rising demand."[x]

As the data shows, the median price of a single family home in the State has increased from approximately $136,000 in 2000 to $264,700 in FY 2004 (most recent data available). Over the past five years, the median housing price has experienced an average annual rate of growth of 14.3 percent.

If the median price of housing were to grow at an average annual rate of 6.0 percent (approximately half the rate of growth in the first half of the decade) for the remainder of the decade, RIPEC projects that it would result in an estimated median price of $386,000 by 2010. One should note that personal income is projected to increase at an average annual rate of 4.0 percent through the remainder of the decade. Given personal income is not projected to keep up with the growth in housing, there are increasing concerns regarding workforce affordability.



## VI. Five-Year Forecast – State Budget

Summary

- RIPEC projects continued operating deficits through the end of the decade, averaging nearly **$145.0 million** each fiscal year;
- Expenditures are projected to increase by 5.6 percent annually during the forecast period while net available revenue is projected to grow by 4.3 percent;
- Spending growth will continue to exceed growth in personal income;
- For every new $1.00 projected to be spent from FY 2006 through FY 2010, grants and benefits will consume $0.45, local aid $0.28, and personnel expenditures will consume $0.26; and
- Medicaid expenditures will continue to be the principal budget driver, increasing by an average annual rate of 8.2 percent through the forecast period and making up nearly 30.0 percent of the State's total general revenue budget.

The following section is a five-year financial projection to identify issues that may arise in the near future. A forecast is designed to provide a baseline fiscal outlook for Rhode Island taxpayers. It is a tool to understand how policy choices may affect the overall financial condition of the State. However, one should use caution when interpreting the data presented. A forecast is only as good as the assumptions it is built upon.

RIPEC projects operating deficits for the State budget to average nearly $142.0 million annually through the end of the decade. Net available revenues are projected to grow at an average annual rate of 4.3 percent, while general revenue expenditures are projected to grow by an average annual rate of 5.6 percent during this period of time. This will create operating deficits that represent nearly 5.0 percent of operating funds over this period of time. Projected operating deficits range from $72.5 million in FY 2007 to nearly $190.0 million by FY 2010. It should be noted that the State's Constitution requires the State to have balanced budgets, so the projected operating deficits must be

**Table 11**
**Projected Budget Statement**

| Statement | FY 2006 | FY 2007 | FY 2008 | FY 2009 | FY 2010 |
|---|---|---|---|---|---|
| Opening Surplus | $40.8 | $0.1 | $0.0 | $0.0 | $0.0 |
| Taxes and Other Sources | 3,165.5 | 3,321.2 | 3,476.1 | 3,634.9 | 3,794.0 |
| Budget Stabilization | (64.1) | (66.4) | (69.5) | (72.7) | (75.9) |
| Net Available | $3,142.2 | $3,254.9 | $3,406.6 | $3,562.2 | $3,718.1 |
| Minus Expenditures | $3,142.1 | $3,327.4 | $3,550.5 | $3,734.5 | $3,907.7 |
| Ending Balance | $0.1 | ($72.5) | ($143.9) | ($172.3) | ($189.6) |
| Operating Surplus/(Deficit) | ($40.7) | ($72.5) | ($143.9) | ($172.3) | ($189.6) |

Source: RIPEC forecast based on Governor's Budget and Enacted Budget (05-H-5270 Sub A) resolved each year. Therefore, as the State balances each of the coming fiscal years, the projected deficits will be affected by those changes that permanently close the gap between revenues and expenditures.

Some of the key growth factors include Medicaid, which is projected to represent nearly 30.0 percent of general revenue spending by the close of the decade, local aid and personnel costs, such as increasing pension and retiree health care benefit obligations. The strengths of the revenue streams remain the personal income tax and the lottery funds. These revenues represent nearly 65.4 percent of the total revenue growth during the forecast period.

*Forecast Assumptions* - One should consider the following risks when developing a forecast – the demographic and social trends, the overall economic outlook, and external actions taken (Federal tax and spending policies, neighboring state actions). Clearly the economy is a moving target in that changes occur often. A forecast cannot anticipate future actions taken by the Federal government or how they might affect the State's revenues and expenditures. Therefore, the forecast assumes current law and relies on existing economic forecast data from the State's Revenue Estimating Conference. The State could enact policies or redirect resources to priorities that are unknown at this time. Additional contract agreements or new bond proposals would also impact the State's financial position.

The following details the assumptions used in the RIPEC forecast. RIPEC has attempted to incorporate projected demographic influences into the forecast where applicable. In developing the forecast, RIPEC attempted to update and incorporate selected assumptions developed by the State Budget Office in the Spring of 2005. RIPEC has also attempted to explain major differences between its forecast and the one presented in the Governor's FY 2006 Budget Request (representing the latest published forecast).

The following analysis forecasts a number of key variables to develop a more comprehensive picture of the State's revenue and expenditure structure. The baseline for the forecast is the FY 2006 Budget as Enacted. It should be noted that the RIPEC estimate was designed to be somewhat conservative in nature in that there are a wide range of variables that are difficult to forecast. The following outlines some assumptions and related data used in the forecast:

*Overall Economic Trends* - The most difficult variable to understand and incorporate into a forecast is the economic forecast. Questions arise as to what stage the United States economy is in, and how will this influence the Ocean State's economic performance. Many currently describe the United States economy in a recovery phase, with the labor market continuing to show signs of growing strength. Major risk factors that are on everyone's mind include natural disasters and the price of oil, which play key roles in both the national economy as well as the State.

In addition, actions by the Board of Governors of the United States Federal Reserve that affect housing and construction activity can affect the State. It should be noted that recent comments by the Chairman of the Federal Reserve noted concerns over the housing market and the potential for a shift in its

**Table 12**
**Rhode Island Economic Forecast - Selected Indicators**

| Indicator | FY 2005 | FY 2006 | FY 2007 | FY 2008 | FY 2009 | FY 2010 |
|---|---|---|---|---|---|---|
| Nonfarm Employment Growth | 1.1% | 1.5% | 1.2% | 0.8% | 0.7% | 0.8% |
| Personal Income | 5.1% | 4.7% | 4.5% | 4.2% | 4.2% | 4.2% |
| Wage and Salary Income Growth | 4.9% | 5.1% | 4.9% | 4.6% | 4.6% | 4.5% |
| Dividends, Interest and Rent | 4.6% | 4.0% | 4.2% | 3.7% | 4.1% | 4.5% |
| Consumer Price Index (CPI) | 2.7% | 2.5% | 2.3% | 2.4% | 2.5% | 2.5% |

Source: May 2005 Consensus Economic Forecast

direction. Neighboring state activity can also play a significant role in determining the economic activity in Rhode Island. Actions taken by Connecticut or Massachusetts to make their taxes more competitive, to attract high wage jobs or to encourage gaming activity can adversely affect Rhode Island's economy and in turn, impact State revenues.

The State's Revenue Estimating Conference (REC) forecasts a number of economic indicators twice a year. These estimates are fundamental to understanding where experts project the State's economy to go through the remainder of the decade. This information sets the stage for how State revenues will perform based on current laws.
The economic forecast developed in May 2005 by the State's Revenue Estimating Conference (REC) reflected a perspective that the Rhode Island economy is performing relatively well. According to Economy.com's testimony, overall investment is growing and job creation remains positive. The REC developed a forecast for non-farm employment where it is projected to peak in FY 2006 at 1.5 percent and then expected to taper off to less than 1.0 percent by FY 2008.

Personal income growth in Rhode Island is projected to decline from 5.1 percent in FY 2005 to 4.7 percent in FY 2006, and is forecast to fall to approximately 4.2 percent through the remainder of the decade. It should be noted that RIPEC's forecast of personal income discussed earlier in this report is slightly less aggressive (4.0 percent average annual growth since FY 2006 verses 4.2 percent forecast by the REC).

Unemployment rates peaked at 5.4 percent in FY 2004 and have since fallen to 4.8 percent in FY 2005 and are projected to fall and remain at approximately 4.4 percent through the balance of the decade. The Consumer Price Index (CPI), a common measure of inflation, is projected to be 2.7 percent in FY 2005. The forecast shows the CPI declining and remaining below 2.5 percent throughout the decade.

<u>*Revenue Forecast*</u> - The FY 2006 Budget as Enacted is the baseline for the revenue projection. RIPEC updated a number of assumptions (including personal income tax growth) developed by the Governor in his FY 2006 Budget Request. It should be noted for example, while the hospital licensing fee requires annual renewal, it has been included in the forecast through FY 2010.

It is unclear what the true impact the recent agreements to further expand the State's video gaming industry will have on both revenues and expenditures. While the agreements indicate net new revenues derived from the expansion of gaming would be used for direct property tax relief, there are currently no statutory requirements to enact these provisions to date. Therefore, RIPEC has not incorporated these additional figures into this forecast.

RIPEC projects that gross general revenue collections will increase at an average annual rate of 4.6 percent from FY 2006 through FY 2010. FY 2006 enacted general revenues total $3,165.4 million, and this is projected to increase to $3,794.0 million by FY 2010, representing a $628.6 million or nearly 20.0 percent increase over this period of time.

Note that the State must allocate 2.0 percent of gross revenue collections into the Cash Stabilization Account, thereby making 98.0 percent of revenue collections available for expenditure. Therefore, RIPEC projects net general revenue collections to increase at an average annual rate of 4.3 percent during the forecast period. Taxes, principally personal income and general sales taxes, represented 78.0 percent of the total general revenue in FY 2006. This is projected to decrease to 76.1 percent by the end of the decade.

Of the $628.6 million in net growth in general revenues from FY 2006 to FY 2010, approximately 66.0 percent ($417.5 million) would be in taxes. The balance of the projected growth ($211.1 million) would primarily occur in lottery proceeds and departmental receipts (a wide range of fees and charges collected by different agencies throughout state government). Total lottery proceeds of $350.5 million in FY 2006 represent 11.1 percent of the net general revenues projected to be collected in FY 2006. In FY 2010, RIPEC projects lottery proceeds to total $543.8 million, or 14.3 percent of total general revenues collected.

**Table 13**
**Summary of Revenue Forecast**
**(Millions)**

| Revenue Source | FY 2006 | FY 2007 | FY 2008 | FY 2009 | FY 2010 |
|---|---|---|---|---|---|
| Personal Income Tax | $1,033.5 | $1,089.5 | $1,142.0 | $1,195.0 | $1,251.3 |
| Business Taxes | 308.6 | 317.0 | 331.2 | 352.6 | 367.1 |
| General Sales Tax | 887.9 | 920.8 | 953.9 | 986.3 | 1,019.9 |
| Other Taxes | 238.5 | 241.2 | 243.9 | 245.9 | 247.7 |
| *Subtotal - Taxes* | *$2,468.5* | *$2,568.4* | *$2,670.9* | *$2,779.8* | *$2,886.0* |
| Departmentals | $307.8 | $314.5 | $321.1 | $327.9 | $334.8 |
| Lottery | 350.5 | 409.7 | 455.2 | 498.0 | 543.8 |
| Other Sources | 38.6 | 28.6 | 28.8 | 29.1 | 29.4 |
| *Subtotal - Other Sources* | *$696.9* | *$752.9* | *$805.2* | *$855.0* | *$908.0* |
| **Total General Revenue** | **$3,165.4** | **$3,321.2** | **$3,476.1** | **$3,634.9** | **$3,794.0** |
| **Change** | | **4.9%** | **4.7%** | **4.6%** | **4.4%** |

Source: RIPEC forecast based on FY 2006 Budget as Enacted and Governor's FY 2006 Budget Request

In FY 2006, personal income tax collections are projected at $1,033.5 million – representing 33.0 percent of all general revenue collections for the State. Based on assumptions discussed below, personal income tax collections are projected to grow at an average annual rate of 4.9 percent over the forecast period. By FY 2010, personal income tax collections are projected to total $1,251.3 million – representing an increase of $217.8 million (21.1 percent).

The forecast for personal income tax collections was developed by using several components of the tax revenues – withholdings, estimated payments, final payments, refunds and accruals. RIPEC adjusted projected withholdings based on wage and salary and personal income growth over the forecast period. The forecast for estimated payments was adjusted using projected changes in dividends, interest and rents, and the balance was forecast based on historic trend information.

Business taxes, which include the State's business corporation tax, taxes on financial institutions and insurance companies, as well as the health care provider assessment are projected to increase by an average annual rate of 4.4 percent over the forecast period. Total business taxes are projected to increase from $308.6 million in FY 2006 to $367.1 million by the close of the decade. This $58.5 million increase would represent a 19.0 percent increase in business taxes over this period of time.

The State has a number of taxes that are considered sales and use taxes. These taxes include the State's general sales tax, motor vehicle and cigarette tax. Overall these taxes are projected to increase from $1,075.8 million in FY 2006 to $1,210.3 million in FY 2010 – a $134.5 million net increase (12.5 percent). The largest of these taxes is the general sales tax, which is the second largest single source of general revenue, representing 28.0 percent of all general revenue collections in FY 2006. RIPEC projects the sales tax to increase from $887.9 million in FY 2006 to $1,019.9 million in FY 2010. This would represent a $132.0 million increase over the forecast period.

Departmental receipts are projected to increase from $307.8 million to $334.8 million by the end of the decade. This represents a $27.0 million net increase in departmental receipts over this period of time. Departmental receipts include a wide range of fees and charges administered by various departments and agencies of state government. These fees are typically levied on those who are being regulated, licensed or fined. The State's hospital licensing fee is included in this category.

Lastly, lottery proceeds are projected to increase from $350.5 million in FY 2006 to $543.8 million in FY 2010, representing a $193.3 million (55.1 percent) increase. Lottery proceeds include lottery games, Keno, and video lottery terminals (VLTs). This particular revenue source brings a number of variables to the forecast that become increasingly difficult to forecast.

The forecast assumes Lincoln Park adds 459 video lottery terminals (VLTs) remodeling at the facility will be completed in 2005. The revenues projected from the installation of these additional VLTs will be first realized in FY 2007. The additional 281 VLTs that have been authorized for the Newport Grand have yet to be installed, and it is unclear when such expansion would take place, and therefore the forecast currently does not include any additional revenues from these VLTs.

As noted earlier, it is unclear what the true impact will be given the recent agreements to further expand the State's video gaming industry. While the agreements indicate net new revenues derived from the expansion of gaming would be used for direct property tax relief, there are currently no statutory requirements to enact these provisions to date. Therefore, RIPEC has not incorporated these additional figures into this forecast.

*Expenditure Forecast* - The State's general revenue budget has grown at a faster rate than both inflation and personal income since FY 2000, and is projected to continue to do so through the remainder of the decade. From FY 2006 - FY 2010, the average annual rate of growth in general revenue spending is projected at 5.6 percent (3.7 percent adjusted for inflation). The average annual rate of growth in personal income in the Ocean State is projected to be 4.0 percent during the same period of time (2.1 percent adjusted for inflation). Inflation is projected to average 2.4 percent over this period of time.
What is driving State spending to consistently exceed overall growth in the economy? There are strong links between the size and characteristics of state population and the levels of state government spending on various service programs. Most recognize economic forces as well as socio-economic and demographic trends (i.e. income levels and age cohorts) play critical roles in the expenditure responsibilities of the State. Other major drivers behind State spending include personnel costs and local aid programs.

Given RIPEC's assumptions, RIPEC projects State general revenue spending will grow at an average annual rate of 5.6 percent from FY 2006 though FY 2010. In other words, the State budget will increase from \$3.1 billion in FY 2006 to \$3.9 billion in FY 2010 – representing an increase of \$766.0 million - or 24.4 percent. Even adjusting for inflation, State general revenue spending would increase by 15.7 percent over the forecast period.

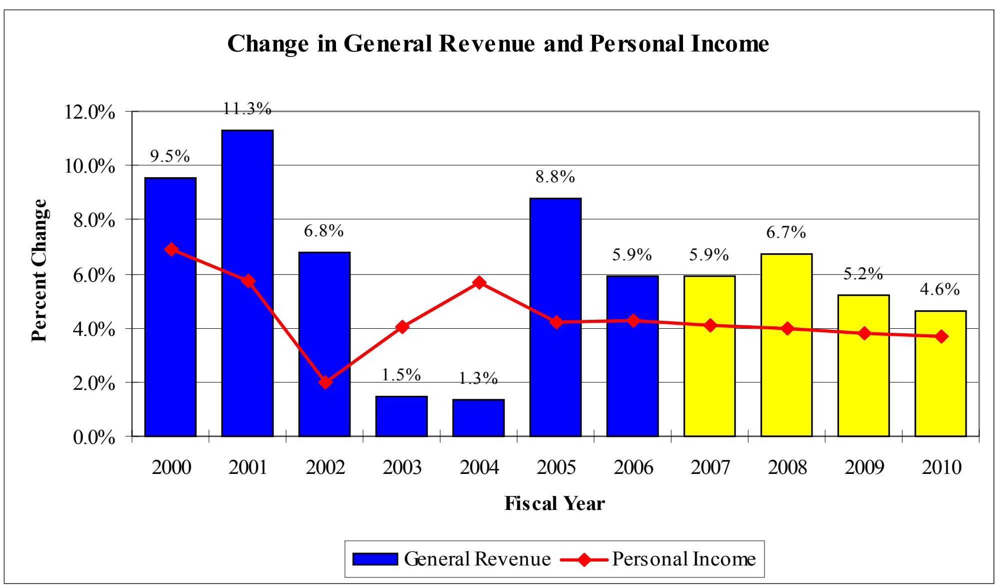


**Table 14**
**RIPEC General Revenue Expenditure Forecast**
**(Millions)**

| Category of Expenditure | FY 2006 | FY 2007 | FY 2008 | FY 2009 | FY 2010 |
|---|---|---|---|---|---|
| Personnel | $806.2 | $847.0 | $927.5 | $966.3 | $1,002.9 |
| Operating | 164.3 | 168.0 | 172.1 | 176.4 | 180.8 |
| Grants | 1,060.2 | 1,136.5 | 1,218.3 | 1,306.1 | 1,400.1 |
| Local Aid | 1,026.1 | 1,080.4 | 1,136.6 | 1,190.1 | 1,242.5 |
| Captial Improvements | 2.1 | 2.2 | 2.2 | 2.3 | 2.4 |
| Debt Service | 83.2 | 93.2 | 93.7 | 93.4 | 79.1 |
| **Total** | **$3,142.1** | **$3,327.4** | **$3,550.5** | **$3,734.5** | **$3,907.7** |
| ***Change*** | | ***5.9%*** | ***6.7%*** | ***5.2%*** | ***4.6%*** |

Source: State Budget Office and RIPEC Forecast

Of the $766.0 million projected increase during the decade, nearly 45.0 percent of the growth can be attributed to grant and benefit programs to individuals. A major driver will continue to be Medicaid expenditures, with projections showing an average annual rate of growth of 8.2 percent through the remainder of the decade. Local aid would account for 28.0 percent of the net growth in state spending and personnel expenditures would represent 26.0 percent of the growth in state spending. Operating and capital and debt service are projected to experience a 1.0 percent combined increase.

**General Operations -** General operations include all personnel and general operating expenditures to support the administrative functions of the State. Personnel expenditures include, but are not limited to, salaries and wages, fringe benefits, and various consultant services. Contract provisions, health care costs and the age and experience of the workforce play important roles in determining the overall burden personnel expenditures place on the budget. Operating expenditures include those expenses that support the day-to-day activities of the State's workforce, to include non-fixed equipment, maintenance, office supplies, lease arrangements, utilities as well as other costs.

In FY 2006, overall general operations represented 30.6 percent of the total general revenue budget. RIPEC projects that while general operation expenditures will increase to $1,183.6 million by FY 2010, the share of total expenditures will decline slightly to 30.3 percent. Overall, general operations expenditures are projected to experience an average annual rate of growth of 5.1 percent. Of the $213.2 million increase in general operation expenditures from FY 2006 to FY 2010, 92.3 percent is attributable to personnel and the 7.7 percent balance was for general operations.

RIPEC projects general revenue personnel expenditures to increase to $1,002.9 million by FY 2010, representing a 24.4 percent increase over the forecast period. This growth represents nearly 26.0 percent of the net growth in total State general revenue spending during the forecast period. In FY 2010, salaries and wages will represent nearly 60.0 percent of the personnel budget, while 34.0 percent of the personnel budget will be used to support fringe benefits. The balance is used to support purchased services (contracts).

RIPEC projects that personnel expenditures will experience an average annual rate of growth of 5.6 percent during the forecast period. RIPEC's forecast included assumptions related to the COLA provisions and the health care provisions included in the recently agreed upon contract. COLAs in FY 2007 and FY 2008 were included at 3.0 percent, and the contributions by employees for health insurance were also incorporated into the forecast (2.5 percent of base wages). Given the contract would be scheduled to expire in FY 2009, RIPEC assumed the 3.0 percent COLA and the same provisions for employee shares for health insurance would continue.

RIPEC also took into account the new schedule for employer contributions for the employee pension fund given the reforms enacted in the FY 2006 Budget. The RIPEC forecast also includes an assumption that as of FY 2008, the State will reflect the actuarially determined annual employer contribution to amortize the unfunded liability with respect to retiree health benefits. Finally, RIPEC included an estimate of what purchased service expenditures are likely to reflect based on historical trends.

RIPEC projects general revenue support for basic operating costs to increase to $180.8 million by the close of the decade, representing an increase of 19.6 percent over the forecast period. Operating expenditures represented approximately 5.2 percent of the State's FY 2006 general revenue budget. RIPEC projects this to decline to 4.6 percent by the end of the decade. Operating expenditure growth will represent 2.2 percent of the net growth in spending over the forecast period. RIPEC assumed that general operating support would increase by the Consumer Price Index through the remainder of the decade (reflecting an average annual rate of growth of 2.4 percent).

**Grants and Benefits -** Often referred to as entitlements, the State's grants and benefits programs represent direct payments to individuals or organizations without taxing authority, either through direct or reimbursement programs. These payments include expenditures related to Medicaid, child care and the Family Independence Program (FIP), Unemployment Insurance and Temporary Disability Insurance, as well as other income support programs administered by the State.

Expenditures for grants and benefits represent the largest category of expenditure in the State budget. In FY 2006, grants and benefits represented 33.7 percent of general revenue expenditures and are projected to increase to 35.8 percent in FY 2010. In Rhode Island, general revenue expenditures for entitlement programs are projected to increase from $1,060.2 million in FY 2006 to $1,400.1 million in FY 2010, increasing by 32.1 percent ($340.0 million) over the forecast period. Some of the programs, such as Medicaid, the Family Independence Program and child care are explained in more detail below.

<u>Medicaid</u> – As shown on Table 15, the major program among grants and benefits is Medicaid. Medicaid is a Federal and state matching entitlement program administered by the states and

**Table 15**
**Change in General Revenue Supported Grants and Benefits**

| | FY 2006 | | FY 2010* | | Change 2006 - 2010 | | |
|---|---|---|---|---|---|---|---|
| Program | Amount | Percent of Gen Revenue | Amount | Percent of Gen Revenue | Amount | Percent Change | Average Ann Change |
| Medicaid | $837.3 | 26.6% | $1,147.6 | 29.4% | $310.3 | 37.1% | 8.2% |
| FIP | 13.3 | 0.4% | 11.9 | 0.3% | (1.4) | -10.5% | -2.7% |
| Child Care | 48.7 | 1.5% | 63.1 | 1.6% | 14.4 | 29.6% | 6.7% |
| All Other | 160.9 | 5.1% | 177.5 | 4.5% | 16.6 | 10.3% | 2.5% |
| Total | $1,060.2 | 33.7% | $1,400.1 | 35.8% | $339.9 | 32.1% | 7.2% |
| **Total State Budget** | **$3,142.1** | | **$3,907.7** | | **$765.6** | **34.3%** | **5.6%** |

*RIPEC projections
Source: State Budget Documents, FY 2006 Enacted and RIPEC Calculations

provides health care coverage to eligible adults and children. The Federal government matches state spending for the services Medicaid covers on an open-ended basis. For program administration, the Federal contribution is set at 50 percent of costs in each state. Higher rates apply to some administrative activities, such as the survey and certification of nursing facilities and fraud investigations and prosecutions.

For medical services, which represent the majority of expenditures, the Federal matching rate (adjusted annually), known as the Federal Medical Assistance Percentage (FMAP), varies by state. The FMAP is based on each state's per capita personal income relative to the Nation as a whole for the three most recent years. States with per capita incomes above the national average receive a lower Federal matching percentage; states with per capita incomes below the national average receive a higher percentage. A state with per capita income at the national average has an FMAP of 55 percent. As one can see on Table 16, Rhode Island is almost at the national average, with a Federal matching rate of 54.7 percent. The operation of the formula is bound by two statutory limits: a minimum of 50 percent and a maximum of 83 percent.

Medicaid is the chief source of funding for long-term care for individuals with limited economic means, health care services for low-income adults with disabilities, health care coverage for qualifying families and their children and pregnant women and infants. About 188,000 people are currently covered under the program in Rhode Island.

**Table 16**
**Federal Medical Assistance Percentage (FMAP)**
**State and Federal Share**
**2000 - 2006**

| Fiscal Year* | State | Federal |
|---|---|---|
| 2000 | 46.2 | 53.8 |
| 2001 | 46.2 | 53.8 |
| 2002 | 47.2 | 52.8 |
| 2003 B. | 45.3 | 54.7 |
| 2003 E.** | 44.4 | 55.6 |
| 2004 B. | 44.1 | 55.9 |
| 2004 E.** | 41.2 | 58.8 |
| 2005 | 44.5 | 55.5 |
| 2006 | 45.3 | 54.7 |

Note: B = Base Year, E = Enhanced Rate
*State Fiscal Year
** Enhanced FMAP rate as part of Federal Jobs & Growth Tax Relief Reconciliation Act of 2003

Source: Rhode Island State Budget Office

Medicaid expenditures have been projected based on enrollment increases, annual inflation in the medical market, and the change in services that people use. The Federal Medicare Prescription Drug, Improvement, and Modernization Act of 2003 will impact Rhode Island's Medicaid spending in future years. Under the Act, dual eligibles (persons who are eligible under Medicaid and Medicare) will receive prescription drug coverage under Medicare Part D as of January, 2006. The forecast does not include any impact of this law on Rhode Island's State budget, nor does it include potential changes based on the President's FY 2006 budget request.

General revenue expenditures for Medicaid are projected to increase from \$837.3 million in FY 2006 to \$1,147.6 million in FY 2010, increasing by 29.3 percent. Of the net growth of total State general revenue expenditures between FY 2006 and FY 2010 (\$765.6 million), Medicaid will account for 41.0 percent (\$310.3 million). For every new dollar projected to be spent between FY 2006 and FY 2010, Medicaid expenditures would account for \$0.41 cents. While in FY 2006 Medicaid accounted for 26.6 percent of the State's general revenue budget, it is projected to increase to 30.0 percent of the general revenue budget by FY 2010.

Medicaid general revenue expenditures are projected to grow at a slower pace in the second half of the decade than in the first half, growing at an average annual growth rate of 8.2 percent between FY 2006 and FY 2010, compared to 8.7 percent between FY 2000 and FY 2005. One possible reason for the slightly slower growth may be slower enrollment growth in the latter part of the decade. One should note the expansion in enrollment due to policy changes between 2000 and 2002. Overall Medicaid enrollment grew by 5.1 percent annually between FY 2000 and FY 2005, and RIPEC projects an average annual growth rate of 2.9 percent from FY 2006 through FY 2010.

In RIPEC's FY 2006 Medicaid report (April 2005), RIPEC projected Medicaid expenditures through Federal fiscal year 2010 by various types of services. The data was presented for the Federal fiscal year (October – September) because expenditure data by services for the State fiscal year (July – June) were not available. In this report, RIPEC projected that acute care will account for two-thirds of the total Medicaid budget and long-term care for 28.0 percent in Federal FY 2010. A trend of concern is the shift in age that will begin to shape Rhode Island's population after 2010 and the relatively high costs per case for long-term care. As noted earlier in the report, the Census projects those of age 65 or older to represent 14.1 percent of the population by 2010, going up to 21.4 percent by 2030.

<u>Family Independence Program/Child Care</u> - RIPEC forecasted Family Independence Program (FIP) and child care slot expenditures by first forecasting costs per cases/slots for FY 2007 through FY 2010 based on a rolling five-year average. Total costs were then determined by multiplying the projected caseload by the cost per case/slot. To determine general revenue expenditures for FIP, RIPEC assumed that the general revenue share of FIP expenditures would remain at the FY 2006 level of 19.0 percent, and the Federal portion would remain at 81.0 percent. In the case of child care slots, RIPEC assumed that the general revenue share of expenditures would remain at 65.0 percent and the Federal share would

remain at 35.0 percent for the reminder of the decade.

One should note that the United States Congress is currently debating reauthorization of the Temporary Assistance for Needy Families (TANF) program. As of October 2005, no action has been taken. Therefore, RIPEC's forecast does not take into account any changes by the Federal government to the program.

Combined costs for FIP and the State-subsidized child care slots are projected to increase from $62.0 million in FY 2006 to $75.0 million in FY 2010. This translates into an average annual growth rate of 4.9 percent. As a percent of total general revenue expenditures, FIP and child care expenditures are projected to remain at 1.9 percent.

When looking at FIP and child care separately, one can see that FIP expenditures supported by general revenue are projected to decline from $13.3 million in FY 2006 to $11.9 million in FY 2010, representing a decline of $1.4 million (10.5 percent decline) during that time period. The decline in expenditures mainly reflects a declining caseload, offsetting a slight increase in cost per case. The caseload is projected to decline from 33,725 in FY 2006 to 28,504 (15.5 percent decline) in FY 2010.

On the other hand, general revenue expenditures for State-subsidized child care slots are projected to increase from $48.7 million in FY 2006 to $63.1 million in FY 2010, increasing by $14.4 million or 29.6 percent) during the forecast period. The increased expenditures reflect a projected increase in the caseload and a slight increase in the annual cost per slot.

All other grants and benefits, mainly Unemployment Insurance and Temporary Disability Insurance, account for the balance of $16.6 million in grant and benefit general revenue increases between FY 2006 and FY 2010. It is projected that general revenue expenditures will increase from $160.9 million in FY 2000 to $177.5 million in FY 2010. As a percent of total general revenue expenditures, all other grants and benefits are projected to decline from 5.1 percent in FY 2006 to 4.6 percent in FY 2010.

**Local Aid -** Aid to local governments includes a wide range of direct aid programs, such as education aid, various municipal aid programs and several public safety incentive benefit programs. These payments go directly to local governmental subdivisions that have both governance and taxation responsibilities.

RIPEC projects general revenue supported local aid expenditures to increase to $1,242.5 million by FY 2010, representing a 21.1 percent increase over the decade. The $216.4 million increase will represent 28.3 percent of the net growth in spending from FY 2006 through FY 2010. Local aid of $1,026.1 million in FY 2006 represented approximately 32.7 percent of the operating budget. RIPEC projects that this will remain essentially unchanged by the close of the decade (31.9 percent).

RIPEC projects local aid expenditures to experience an average annual rate of growth of 4.9 percent during the forecast period. RIPEC assumed that direct education aid would increase by 3.7 percent annually during the forecast period (requiring $760.4 million in direct State education aid). Charter schools are expected to continue expanding, with a projected growth rate of 5.0 percent annually. While the forecast does incorporate the reforms of the pension changes enacted in the FY 2006 Budget as Enacted, the State will continue to see significant growth in teacher pension costs.

In non-school local aid, the two programs of note include the State's general revenue sharing program and the State's program to phase out the excise tax on motor vehicles. RIPEC has assumed that the State will further increase the amount of auto value exempted by the State by approximately $500 per year, and that the State will continue on its scheduled program to increase the General Revenue Sharing Program.

**Capital Improvements and Debt Service -** Debt service represents the State's payments on long-term obligations. These include general obligation bonds, the debt for the Rhode Island Public Building Authority, Certificates of Participation and other third-party leasing arrangements, and debt for the Convention Center Authority. Capital improvements represent minor improvements to buildings or roads, as well as any acquisition of fixed equipment. Approximately 2.7 percent of the FY 2006 operating budget is allocated to support debt service and capital improvements. This is projected to decline to 2.1 percent by the close of the decade. Note that the State has a separate capital budget for the purchase, building and leasing facilities, roads, and other infrastructure using long-term financing arrangements.

Debt service and capital improvements that are included in the operating budget represent the smallest portion of the operating budget. Together, the two categories of expenditure are projected to total $81.4 million by FY 2010, representing 2.1 percent of the total general revenue budget. Over the forecast period, RIPEC forecasts that capital and debt service expenditures will experience an average annual rate of decline of 2.2 percent.

One area of particular concern is shifting debt service from the general fund to the Capital Fund. The amount shifted is consuming a greater share of the available funds that would otherwise be used to support capital projects. While the Governor has stated in his most recent five-year forecast that he intends to shift all of the debt service currently supported by the Capital Fund back to the General Revenue Fund in FY 2007, this may be difficult to achieve. Therefore, RIPEC has assumed that the portion of debt service currently supported by the Capital Fund (approximately $34.4 million) will remain in the Capital Fund. It should be noted that this represents a significant deviation from the Governor's five-year forecast, representing less expenditure demand from debt service obligations. Therefore, RIPEC's forecast reflects overall projected operating deficits that are not as large as they would otherwise be if this shift were to occur.

# VII. References

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