



Background Briefing

STATE BUDGET OVERVIEW

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January 2015

State Appropriation Fund Source Definitions

- 1. Federal Funds:** Federal grant or match revenue; generally dedicated to specific programs or purposes.
- 2. Local/Private Funds:** Revenue received from local units of government and private, non-governmental entities for specific services or purposes.
- 3. State Restricted Funds:** State revenue restricted by State Constitution, state statute, or outside restriction that is available only for specific purposes. Includes most fee revenue. Largest such fund is the School Aid Fund.
- 4. General Fund/General Purpose (GF/GP):** Unrestricted General Fund revenue available for basic state programs and other purposes determined by the Legislature.

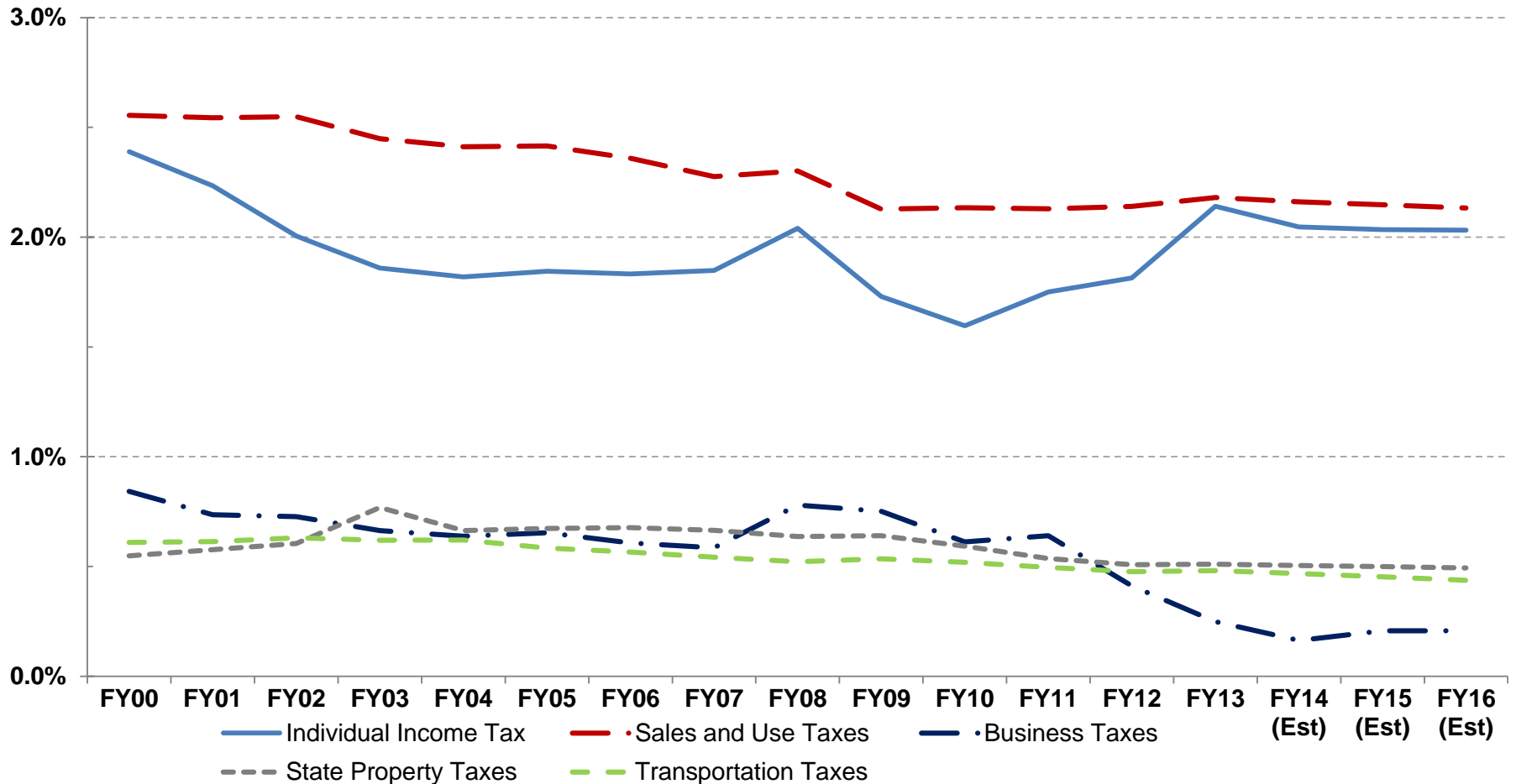
Adjusted Gross Appropriations: Total state appropriations from all fund sources. Excludes funds appropriated twice in state budget through interdepartmental grants (IDGS) or intradepartmental transfers (IDTs).

State Source Appropriations: Appropriations from state-level revenue sources: State Restricted plus GF/GP.

LONG-TERM REVENUE TRENDS

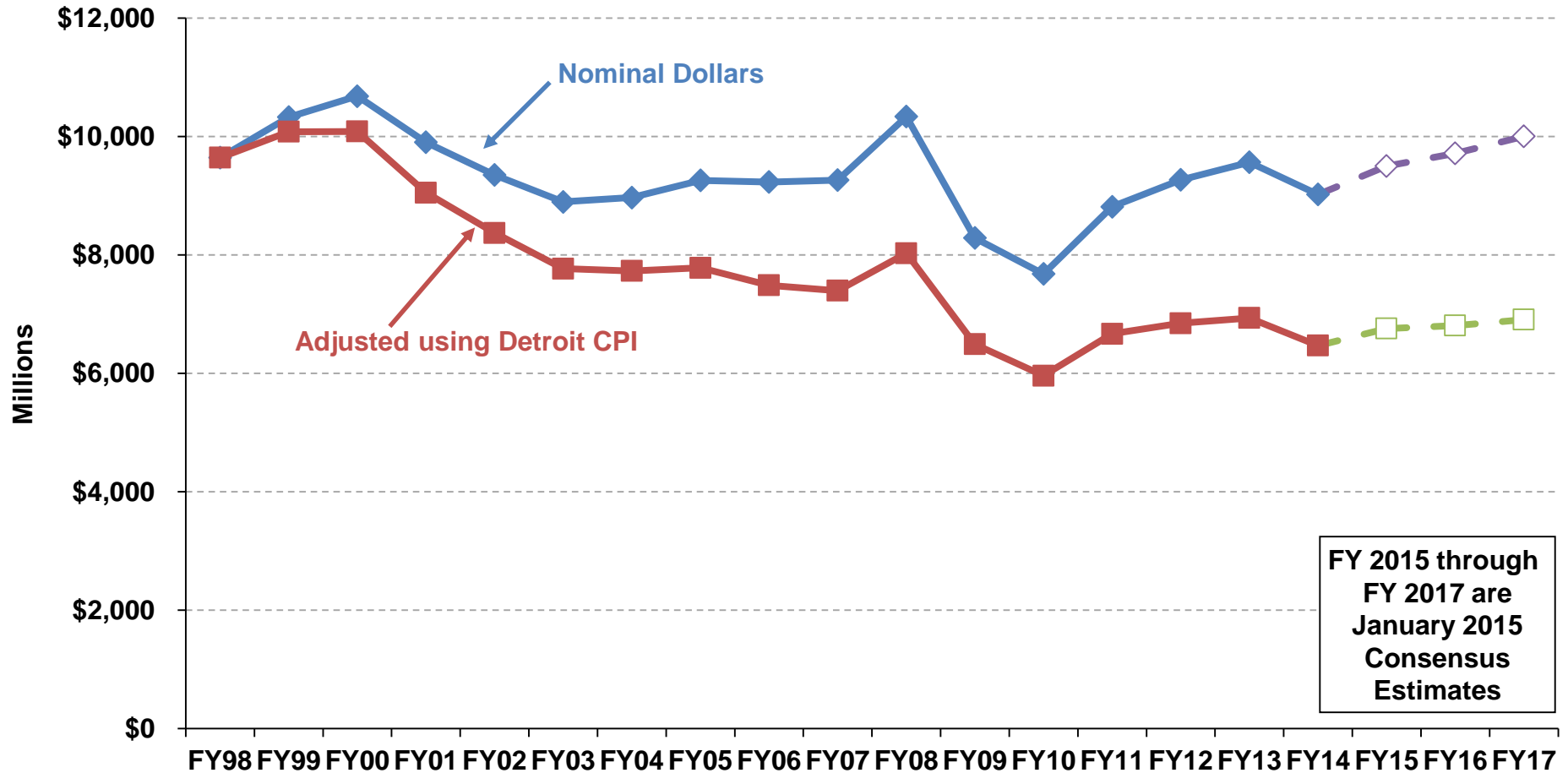
Major State Taxes as a Percentage of Michigan Personal Income

Recent growth in state revenue has been driven by the income tax. Other major state taxes have declined as a percentage of state personal income as a result of economic trends and/or tax policy decisions.



GF/GP Net Revenue

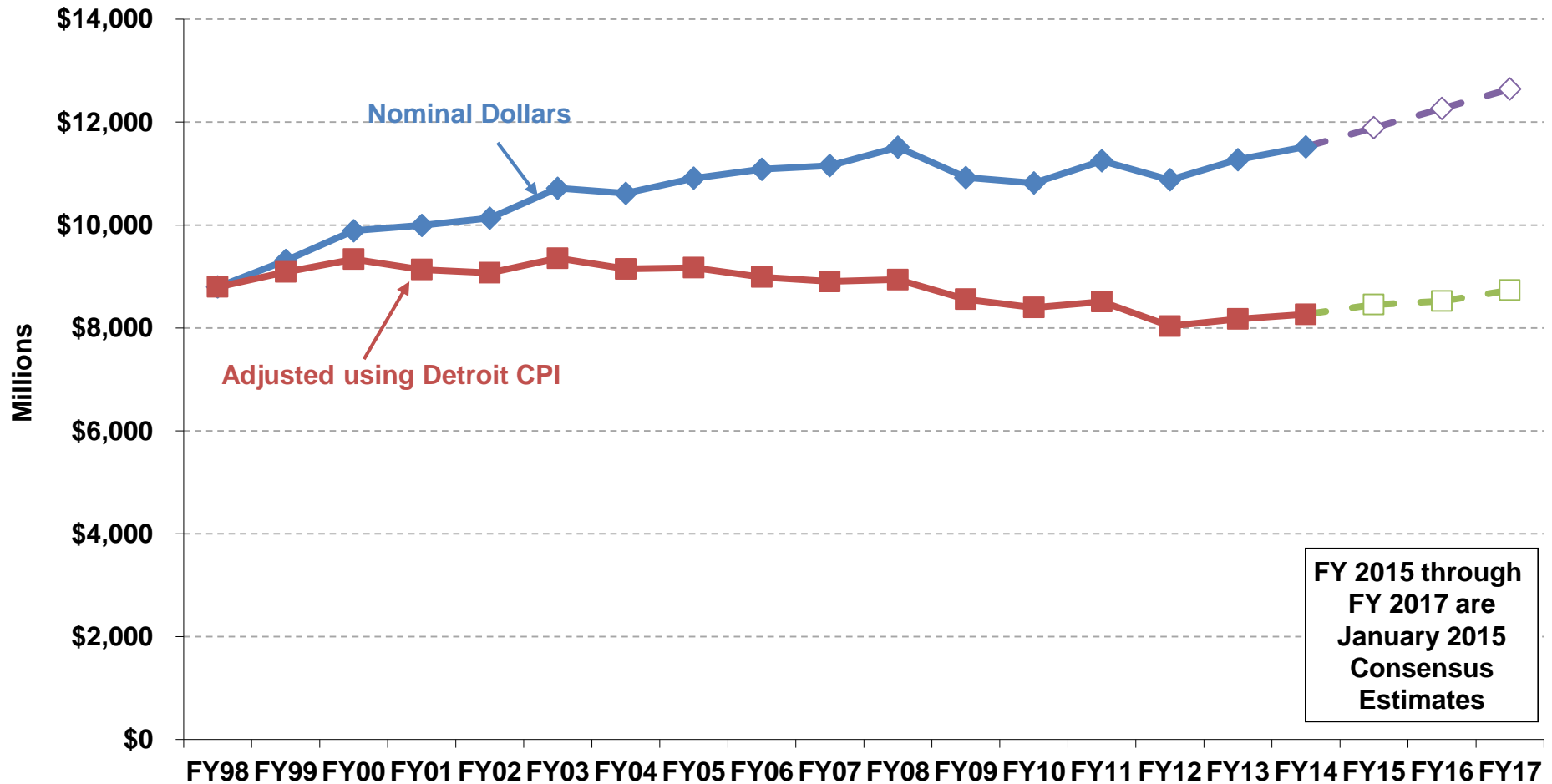
Nominal GF/GP revenue has grown 24% from FY 2010 to FY 2015 but remains below previous peaks. Adjusted for inflation, FY 2015 revenue is 33% below the FY 2000 level.



Note: For consistency, revenue figures for years prior to FY 2010-11 have been adjusted to include sales tax revenue previously designated for statutory revenue sharing.

School Aid Fund Net Revenue

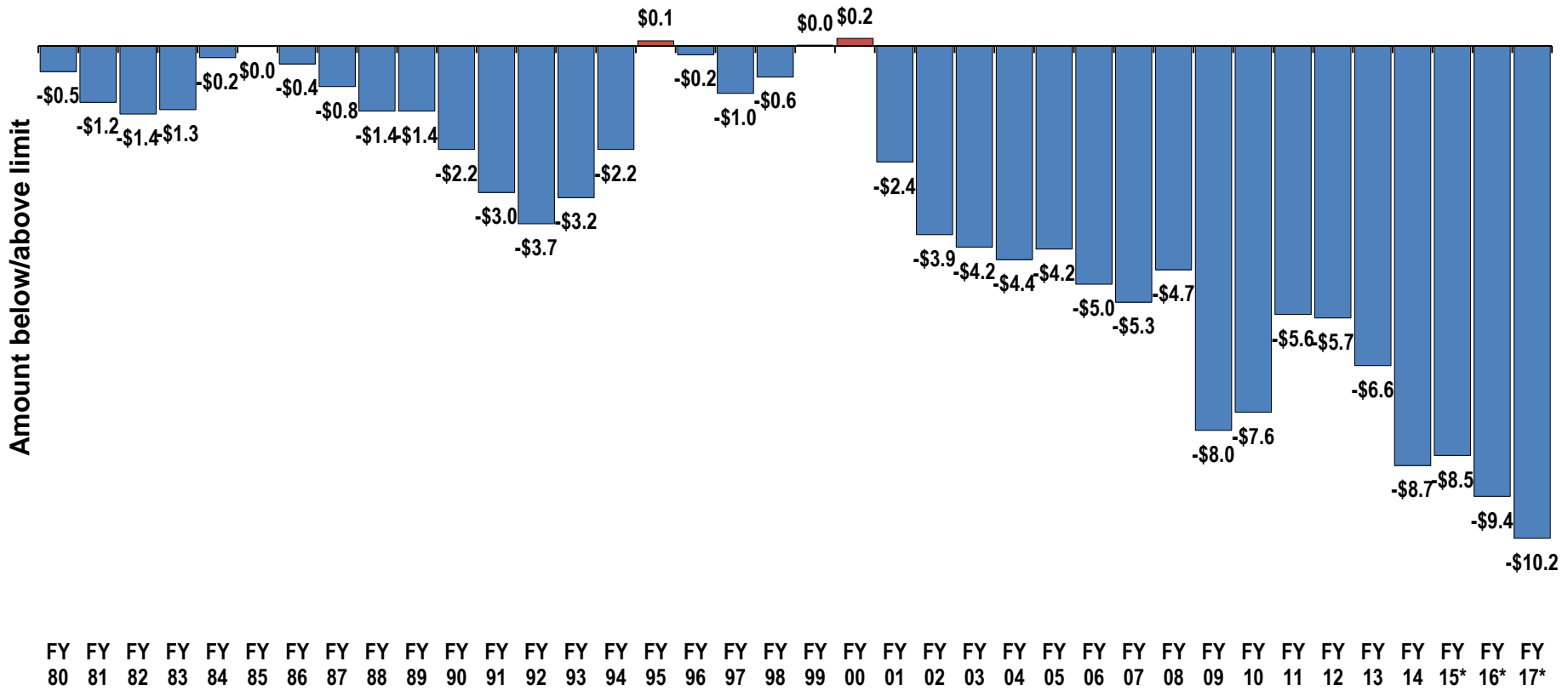
Nominal SAF revenue has grown 9.3% from FY 2012 to FY 2015. Adjusted for inflation, however, FY 2015 revenue is 9.5% below the FY 2000 level.



Constitutional Revenue Limit

(Billions of Dollars)

Total state tax and other revenue collections are \$8.5 billion lower than the limit set in the State Constitution (9.49% of state personal income) for FY 2015.

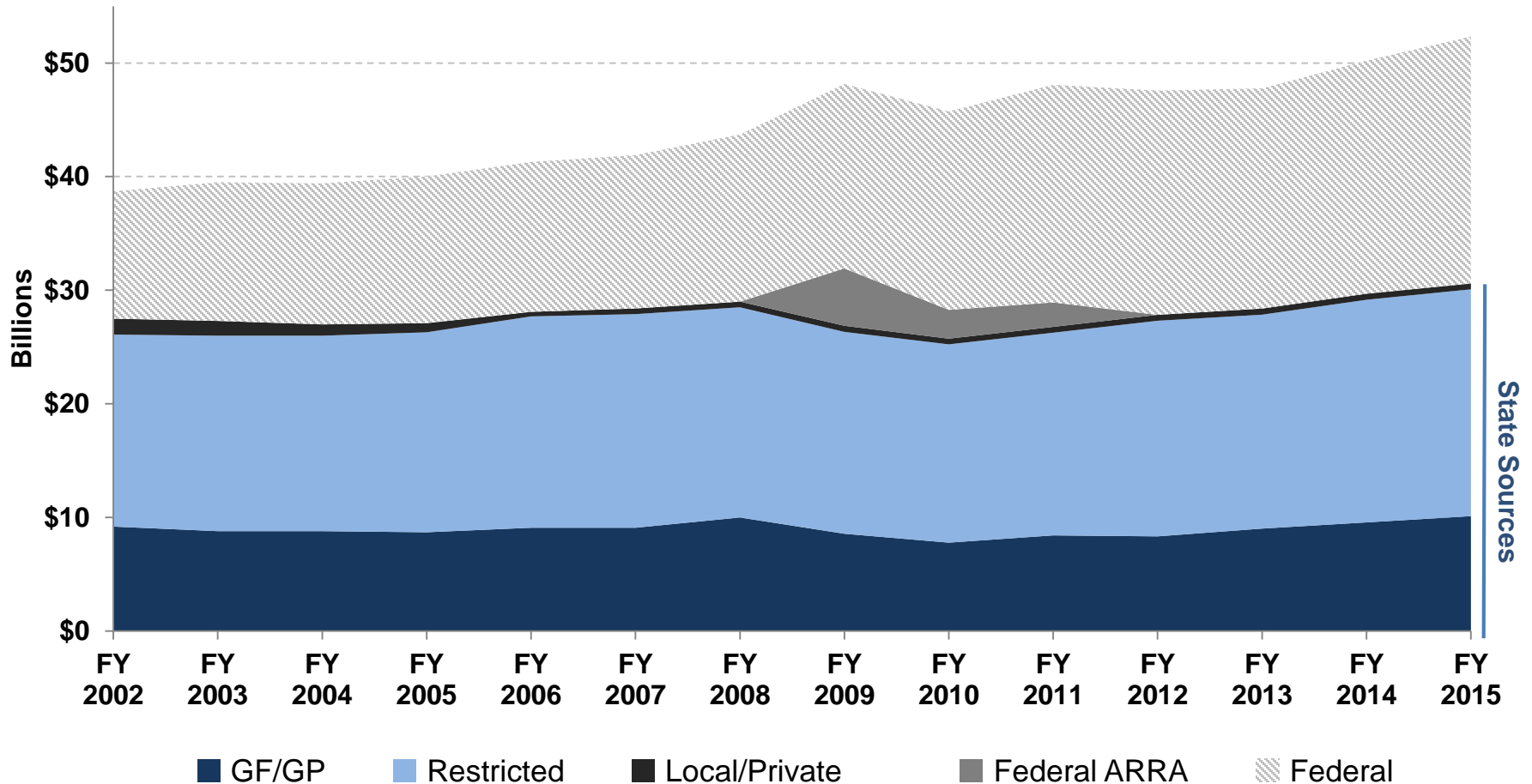


*January Consensus Estimates

LONG-TERM BUDGET TRENDS

Total State Appropriations

While total appropriations have grown 35% since FY 2002, appropriations from state sources have grown just 15%. State budget growth has been driven mainly by increases in available federal funds.

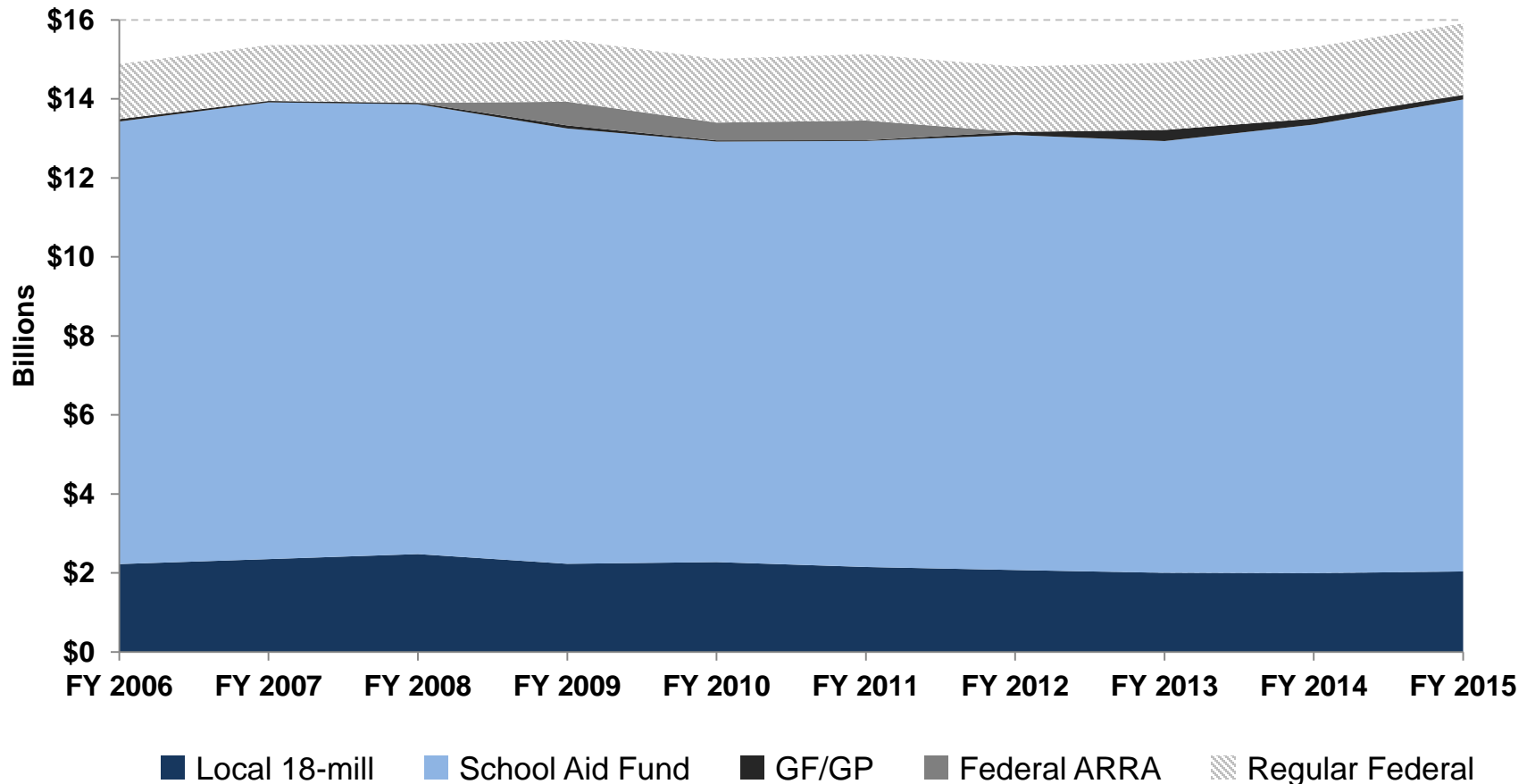


ARRA: Federal American Recovery and Reinvestment Act of 2009

School Aid Funding

Local 18-mill Levy and State Appropriations

Excluding federal funds dedicated for specific purposes, total FY 2015 funding for schools is now slightly above the previous FY 2007 peak (not adjusted for inflation). Recent increases have included significant funding for retirement costs and other categoricals.

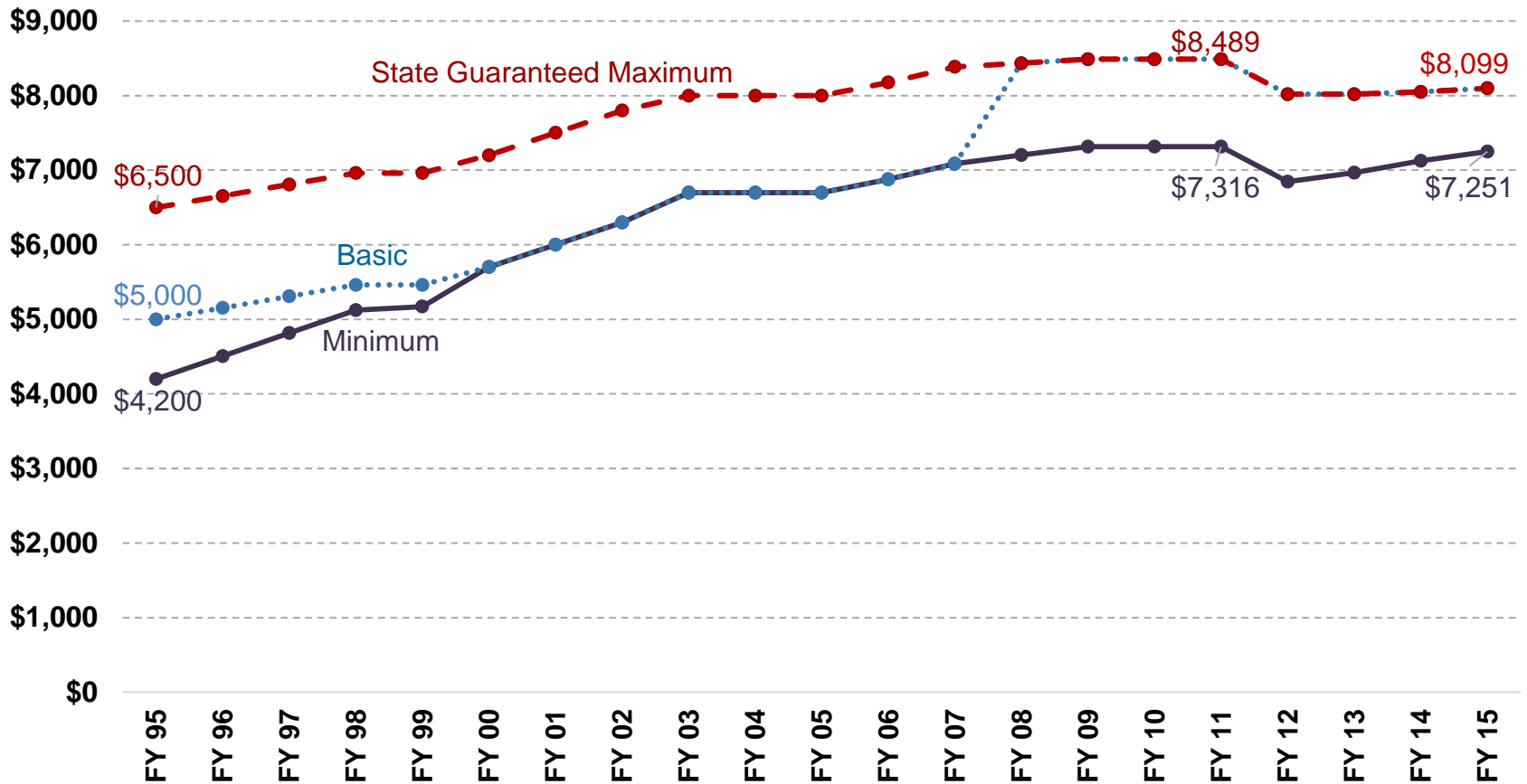


ARRA: Federal American Recovery and Reinvestment Act of 2009

Foundation Allowance History

Growth Since Proposal A

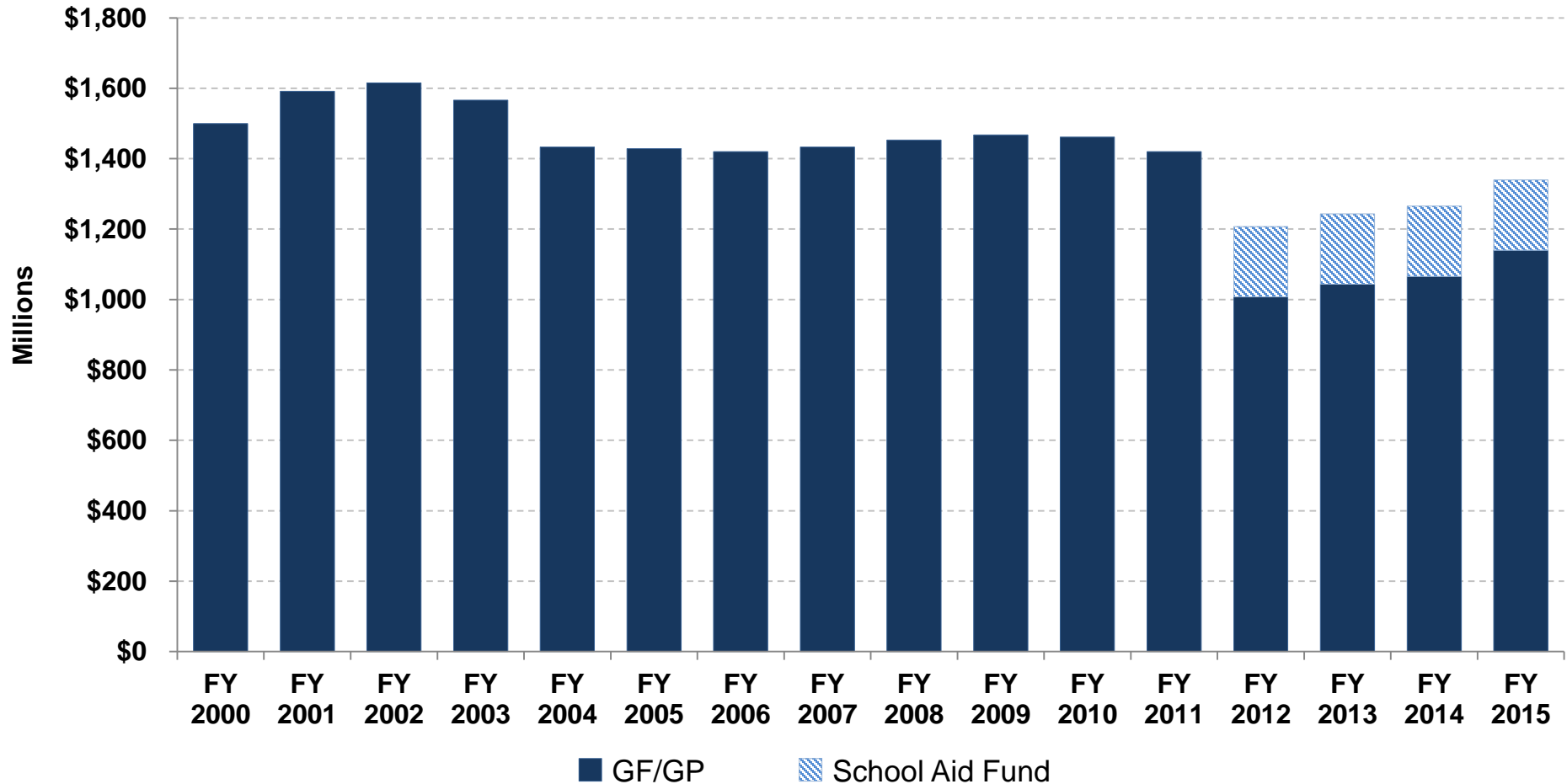
The FY 2015 foundation allowance for schools at the Minimum level is \$65 below the FY 2010 peak. For schools at the State Maximum level, it's \$390 below the FY 2011 peak. The "equity gap" between the two is down to \$848 per pupil.



Note: Does not include the foundation allowances of 37 hold harmless districts that are allowed to collect additional local millage revenue to maintain statutory foundation allowances above the State Guaranteed Maximum.

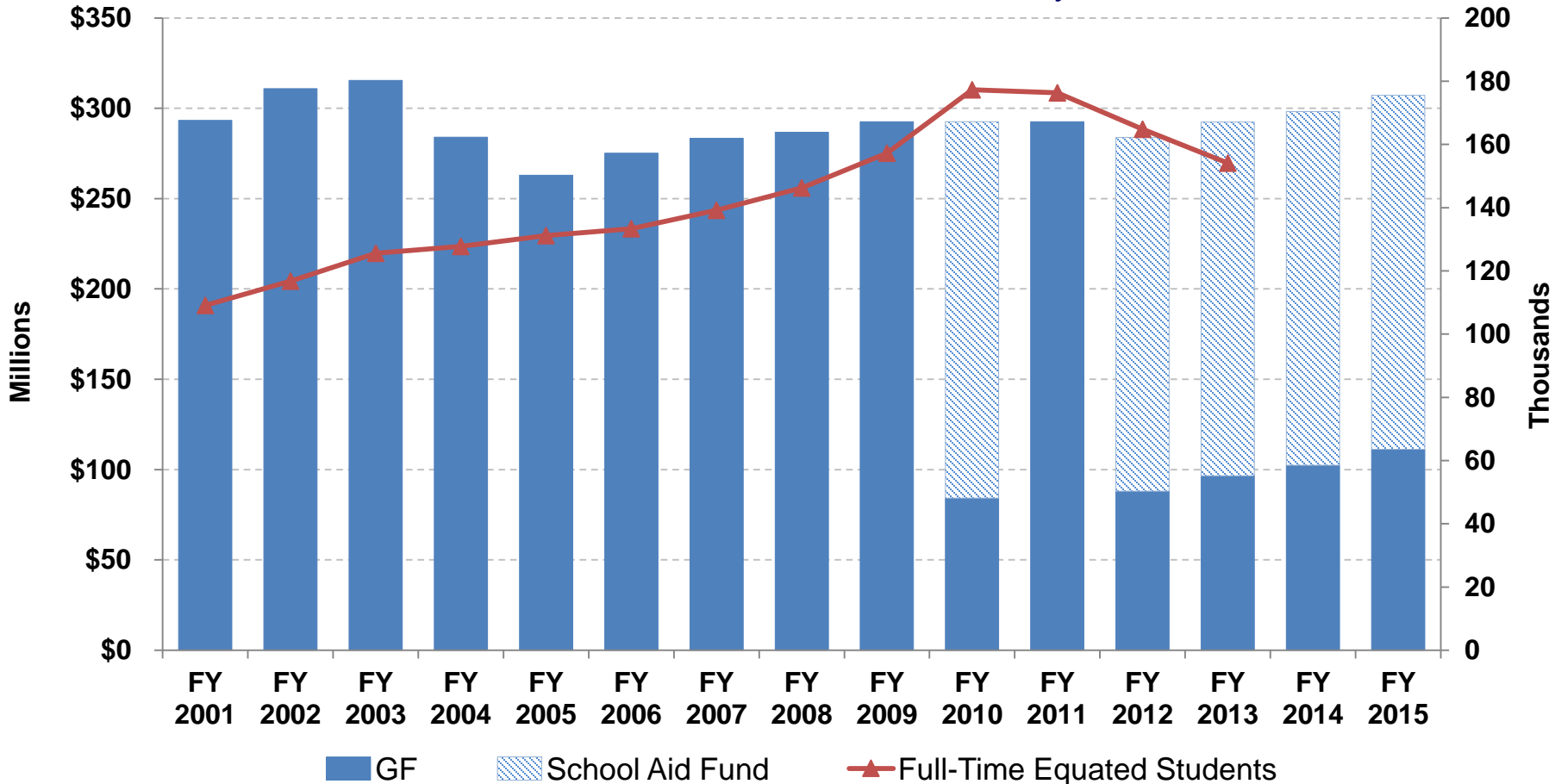
State Appropriations for Public University Operations

State support for public universities has increased by \$133 million (11%) since FY 2012, but remains \$276 million (17%) below the FY 2002 peak.



Community Colleges Appropriations and Enrollment

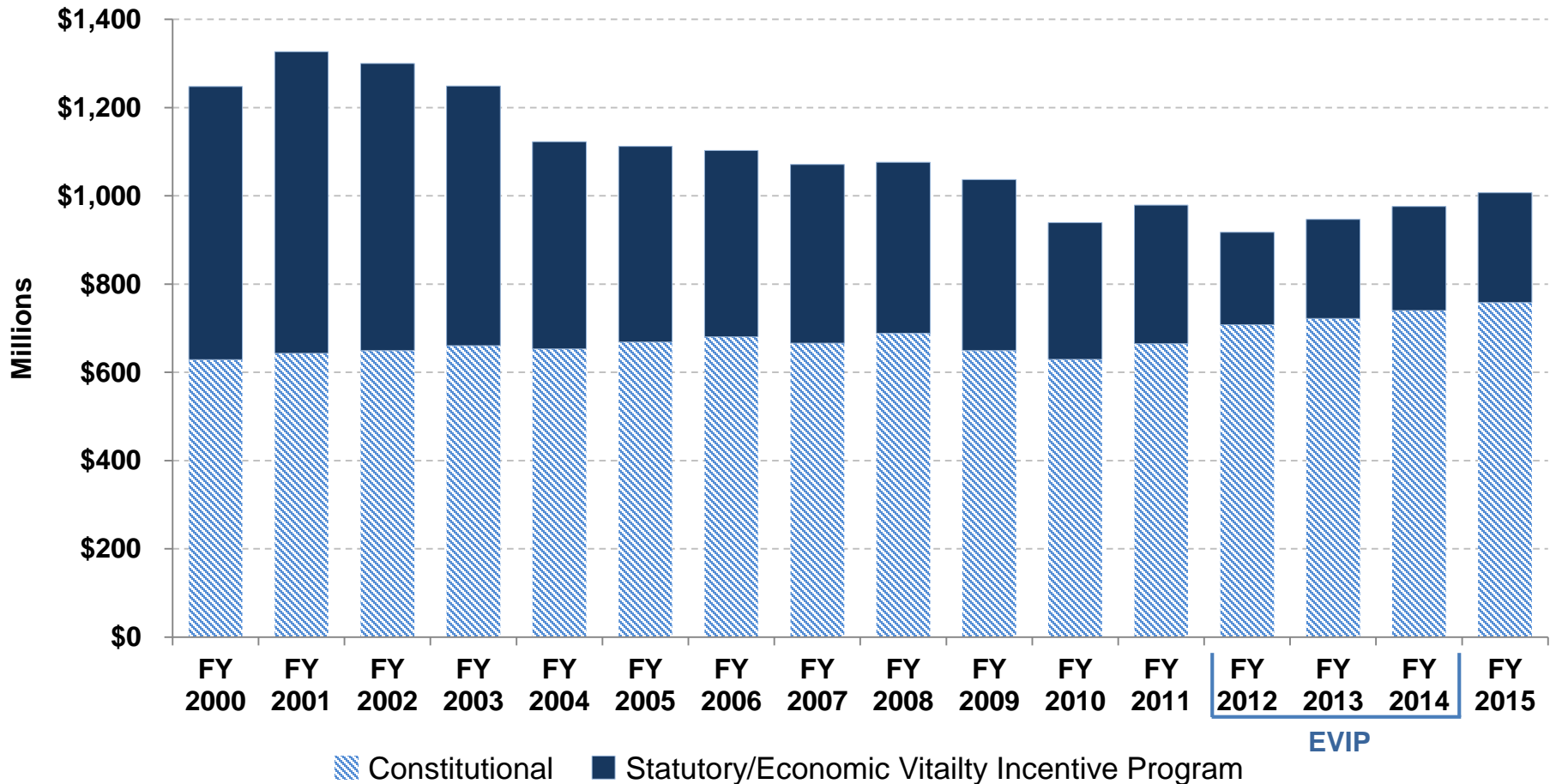
Despite recent growth, state support for community college operations remains slightly below the FY 2003 peak. Enrollment grew rapidly during the 2000's but has tailed off more recently.



Note: Excludes funding added in recent years for retirement rate cap; funds flow through to retirement system.

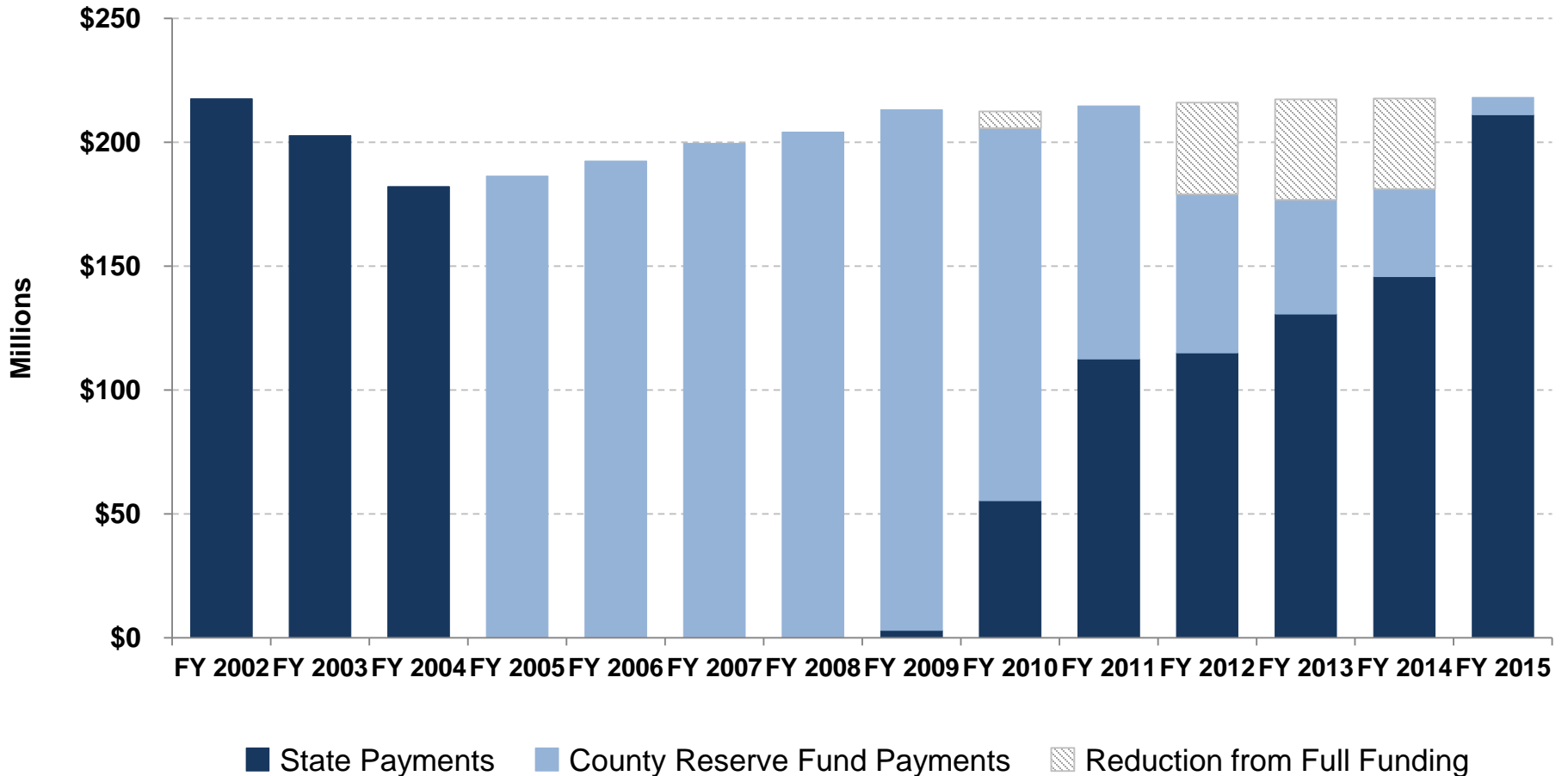
Revenue Sharing to Cities, Villages, and Townships (CVTs)

Per-capita constitutional payments to CVTs have grown consistent with sale tax revenue growth. Discretionary payments remain \$435 million below the FY 2001 peak; reductions have helped balance the GF/GP budget.



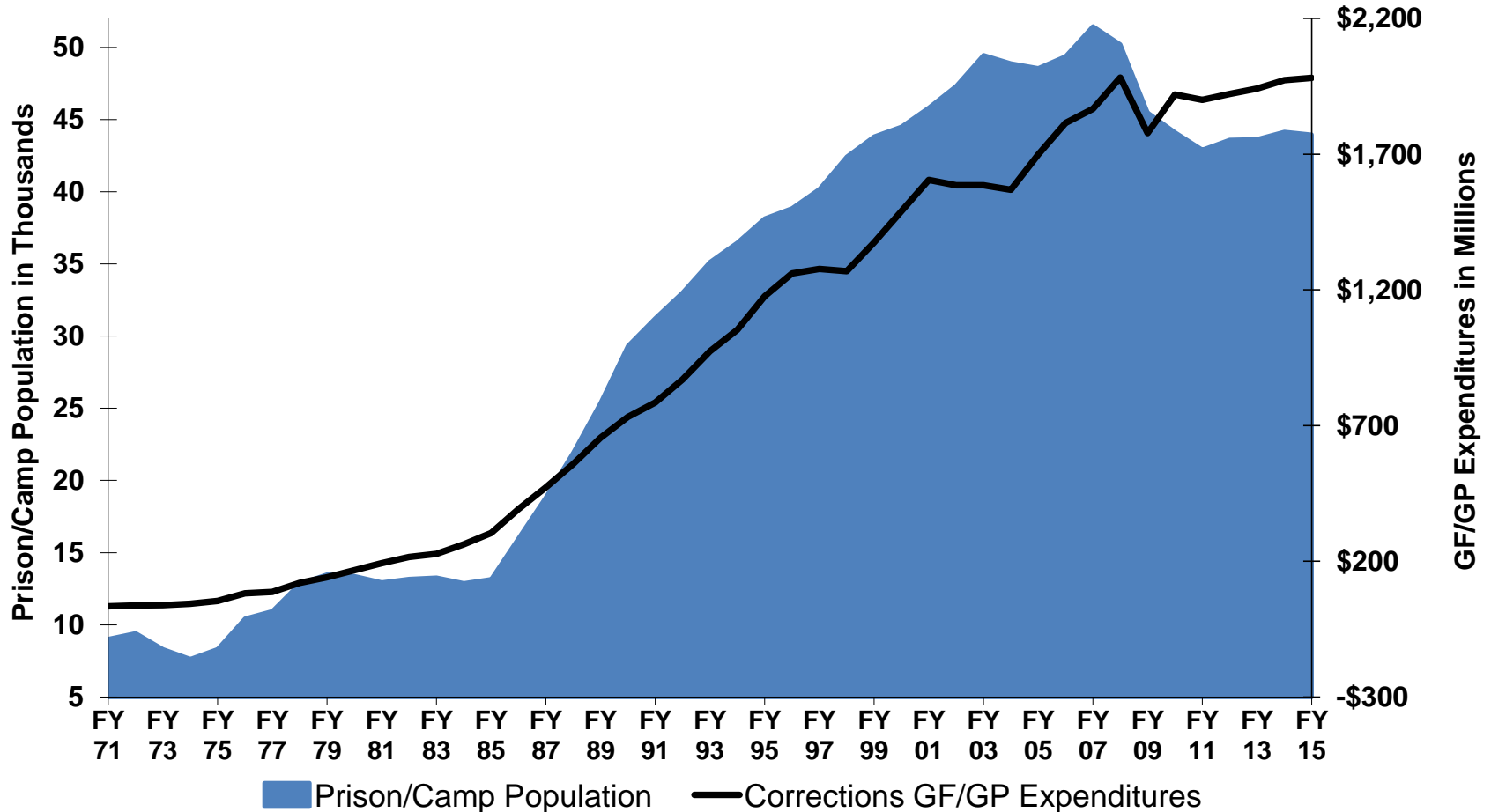
Revenue Sharing to Counties

The reserve fund mechanism allowed for inflationary growth in county payments from FY 2004 to FY 2011. After a period of underfunding, FY 2015 funding to counties is restored to full funding relative to reserve fund payments.



Corrections Budget Increases

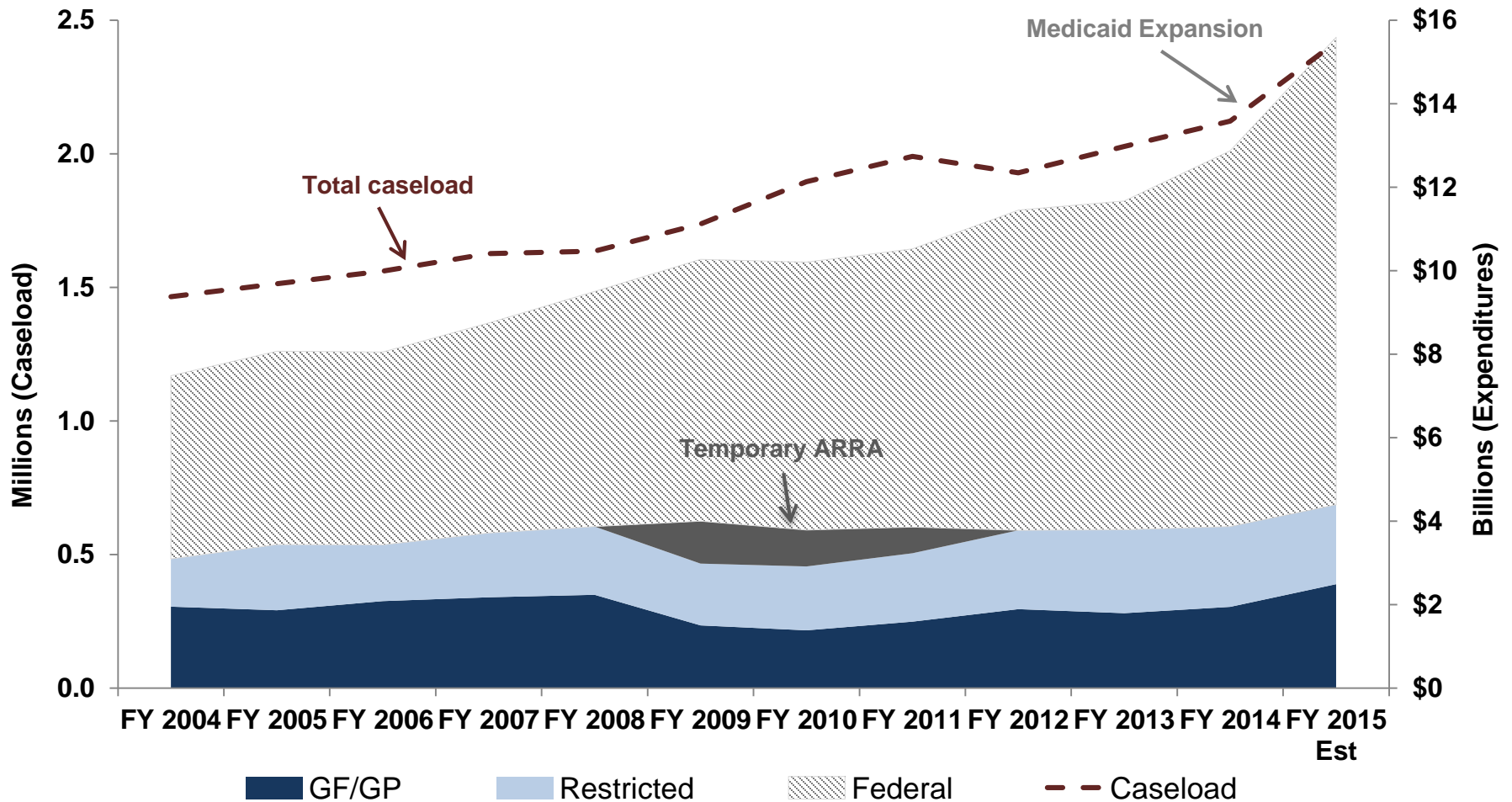
Over the long term, corrections costs have grown consistent with prison population. Increases have moderated in recent years as the population has been reduced. The Corrections budget would have decreased over the last several years if not for the costs of paying down retirement liabilities.



Note: Fiscal Year 2008-09 reflects GF/GP reduction due to appropriation of temporary federal ARRA funds.

Medicaid Expenditures

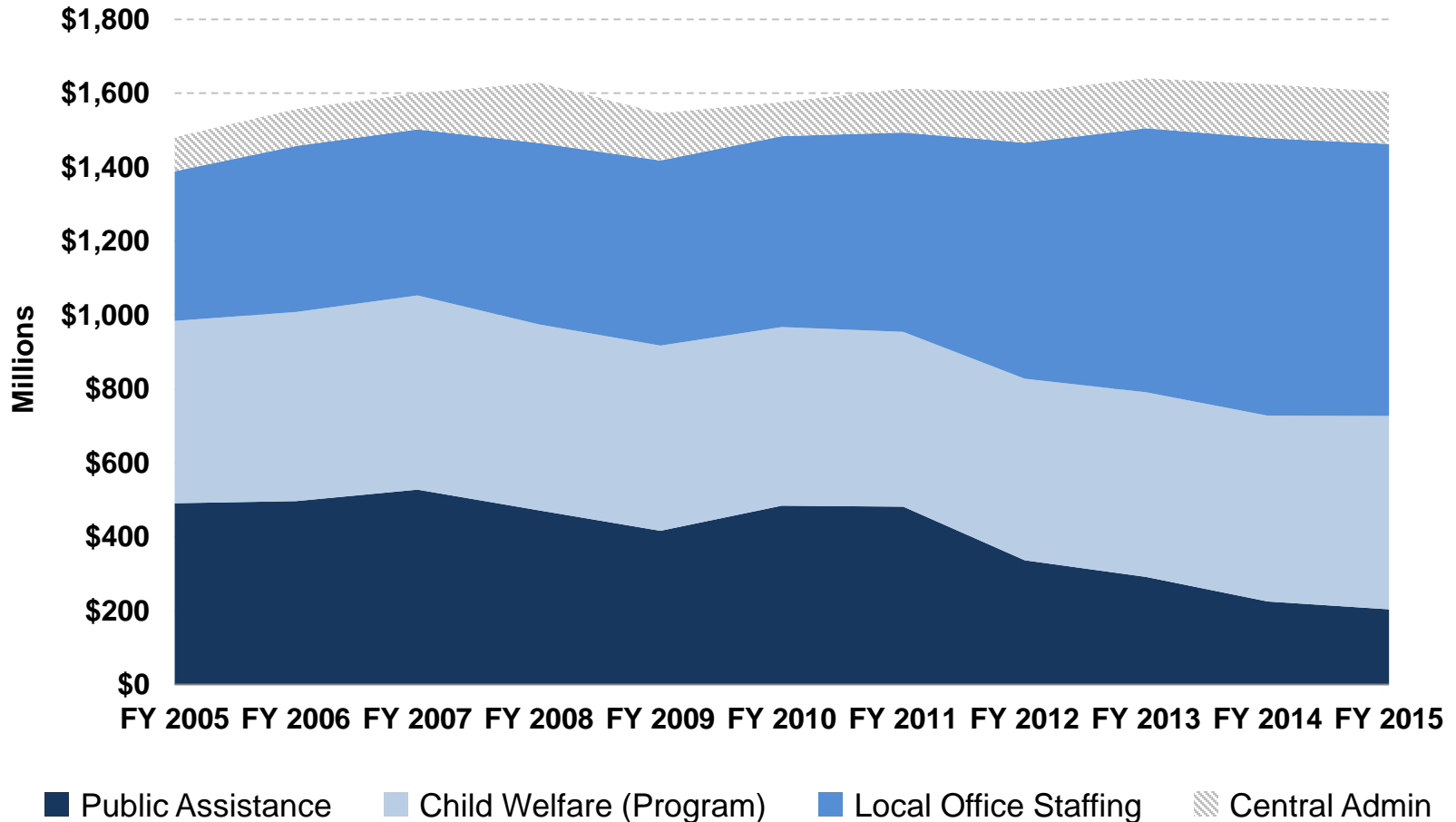
The state's total Medicaid caseload has increased by 65% since FY 2004, driving substantial growth in total Medicaid expenditures. Increases in costs per enrollee and state match requirements, however, have been relatively modest.



ARRA: Federal American Recovery and Reinvestment Act of 2009

Human Services Funding

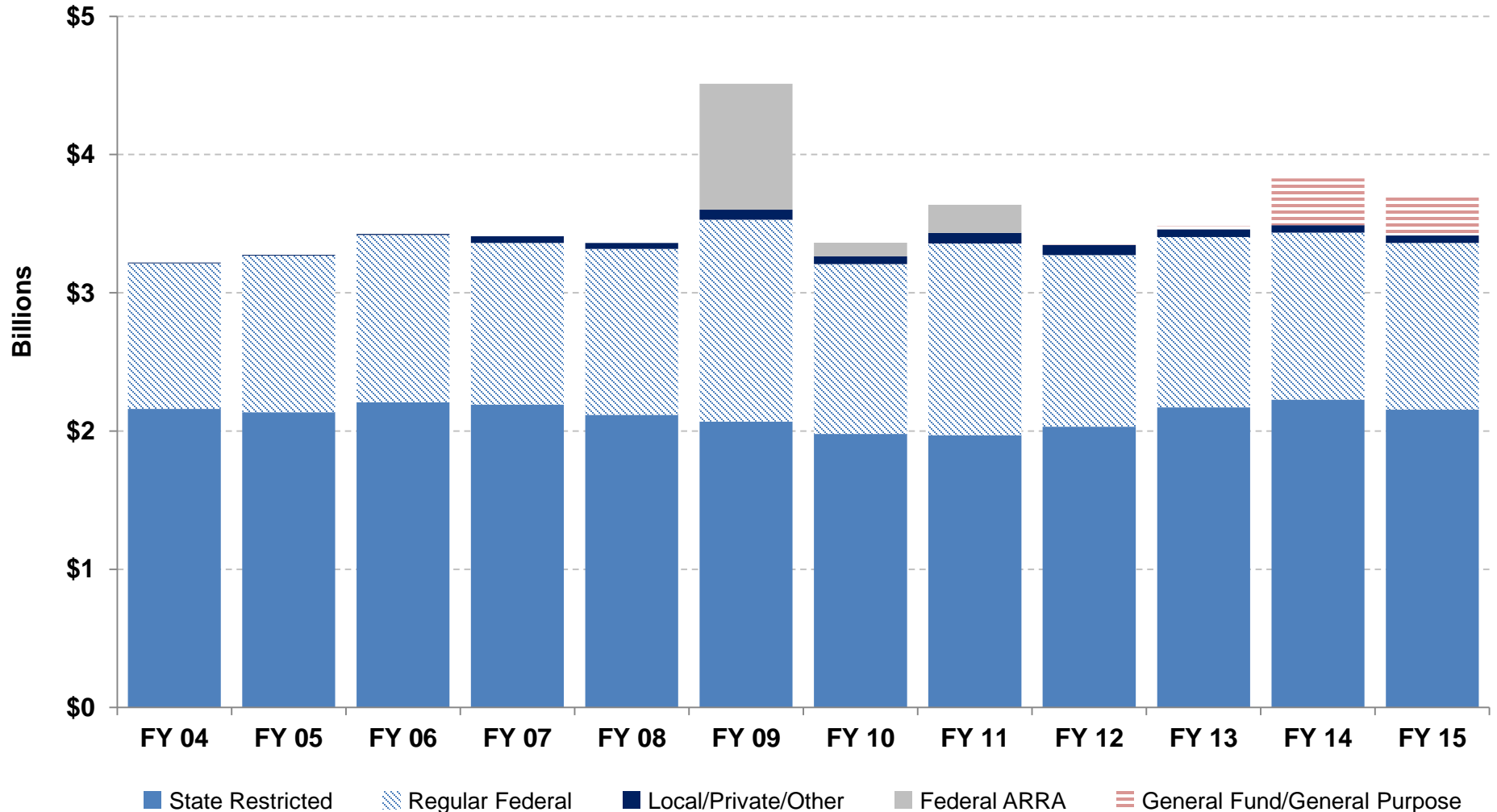
Combined GF/GP and TANF funding for Human Services has been flat in recent years. Public Assistance has declined markedly due to implementing time limits on cash assistance and caseload reductions, while Local Office Staffing has increased due to child welfare settlement staffing enhancements and retirement liability costs.



Note: Figures exclude one-time funding for low income energy assistance in FY 2013.

Michigan's Transportation Budget

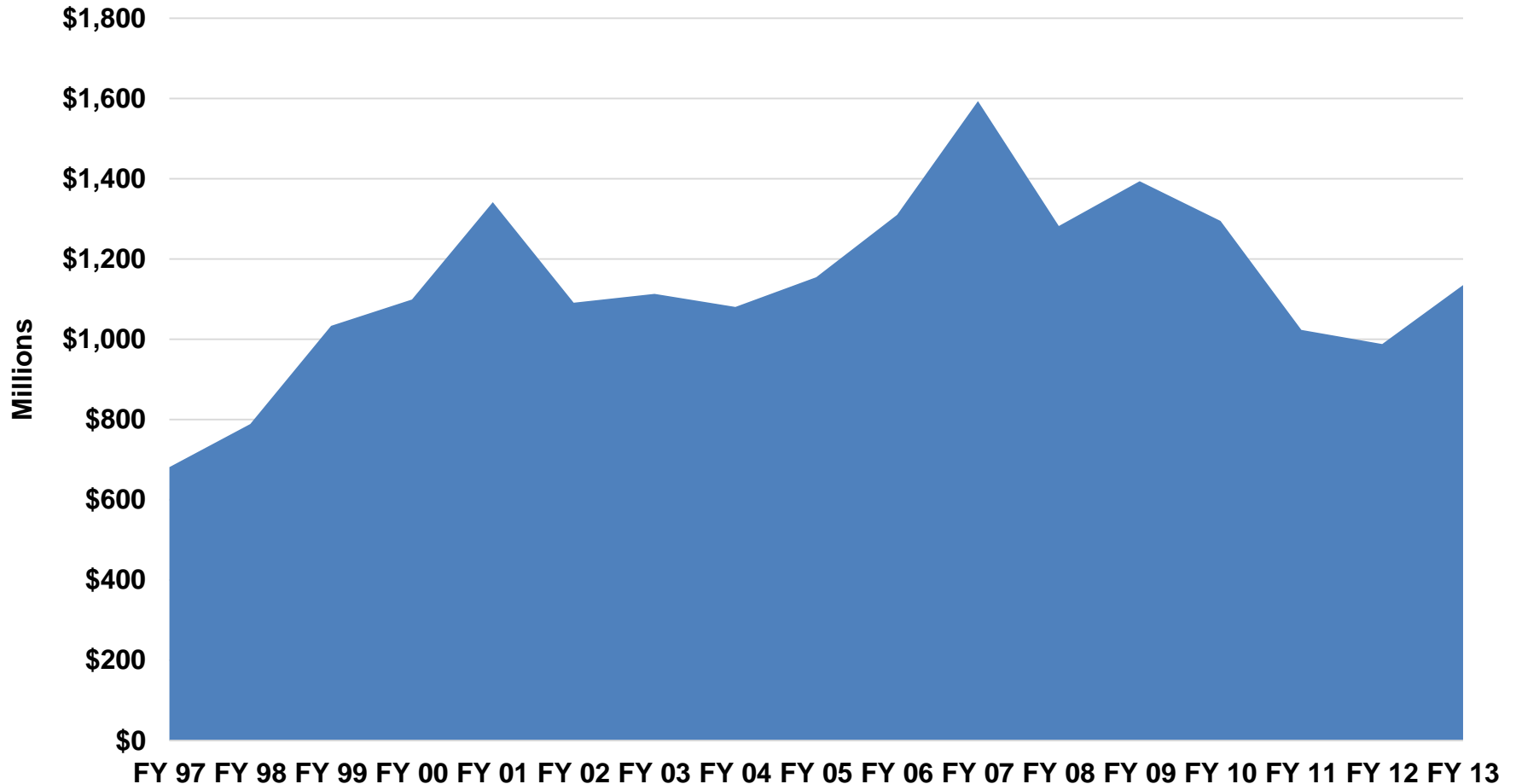
Excluding temporary federal stimulus funds and recent GF/GP allocations, total funding for transportation purposes has experienced minimal growth over the last decade.



ARRA: Federal American Recovery and Reinvestment Act of 2009

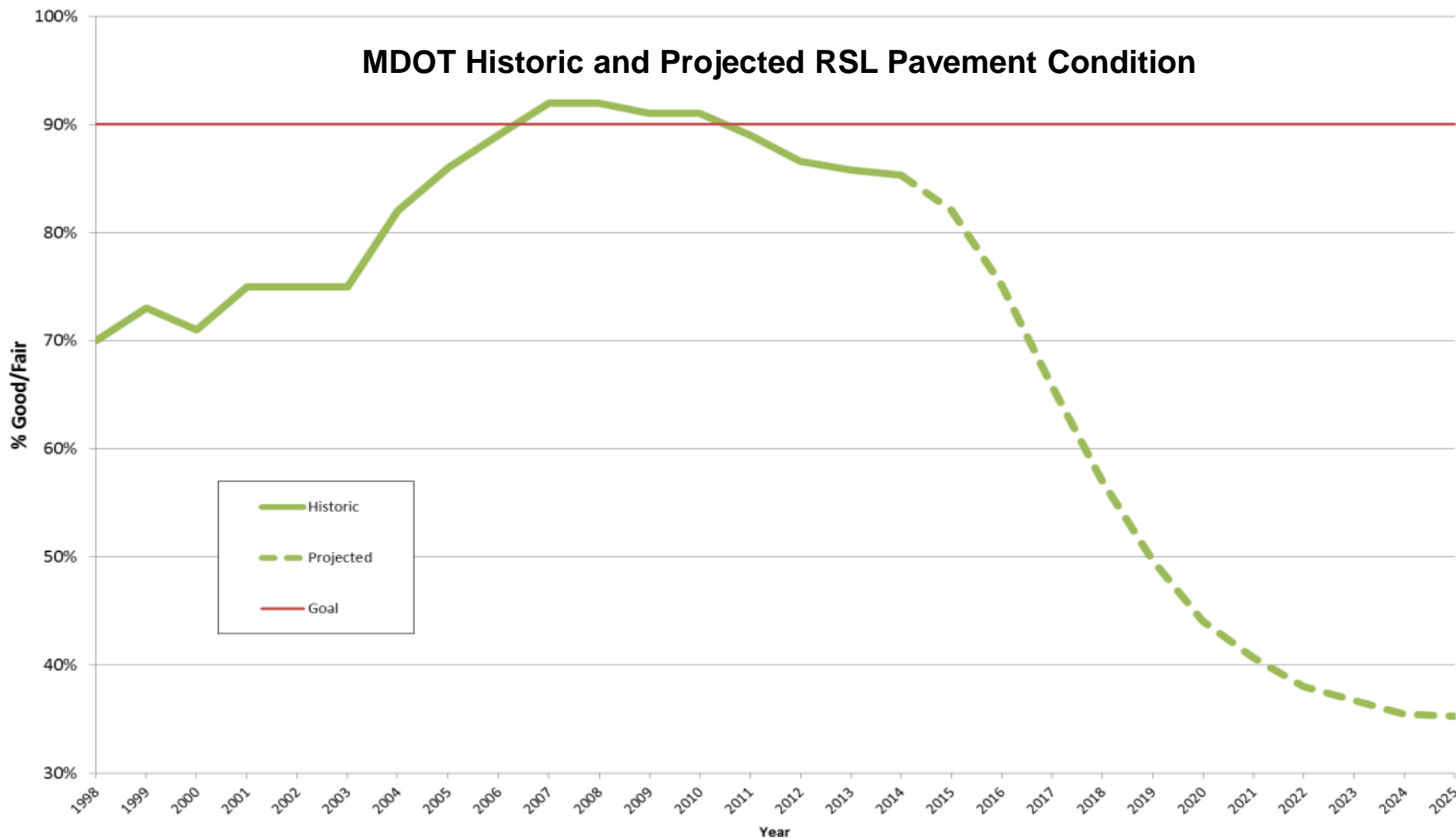
Department of Transportation Construction Contract Awards

Previous peaks in contract awards (State/Local/Aero/Transit/Rail) were driven by the 1997 gas tax increase, debt financing (2001 and 2007), and temporary federal ARRA funds (2009/2010).



State Trunkline Pavement Condition Combined Freeway and Non-Freeway

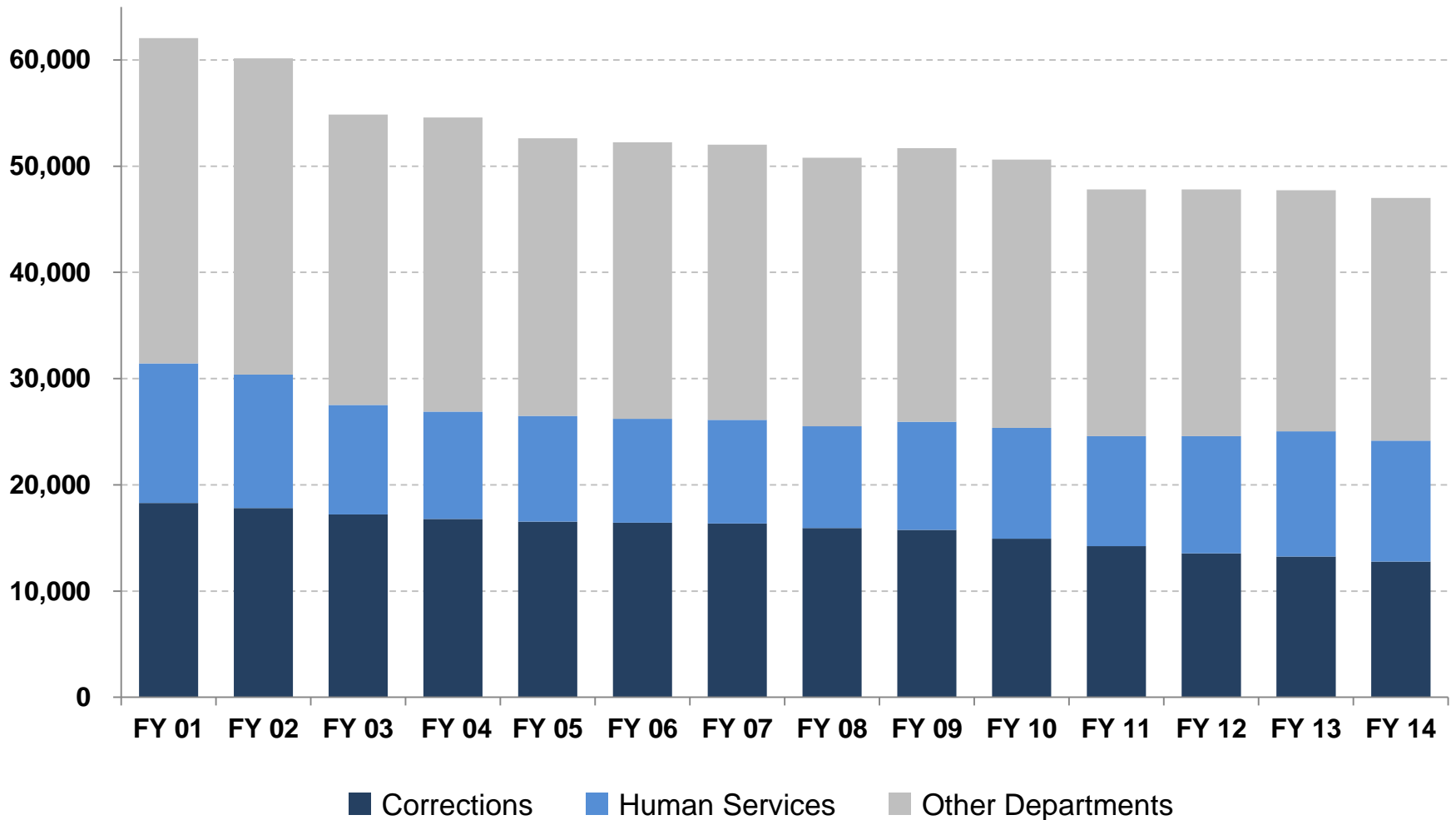
Current revenue sources dedicated to transportation, mainly fuel and vehicle registration taxes, are insufficient to maintain the state's road system in fair/good condition.



Source: Michigan Department of Transportation, 2014-2018 Five-Year Transportation Program

Total Classified Employees

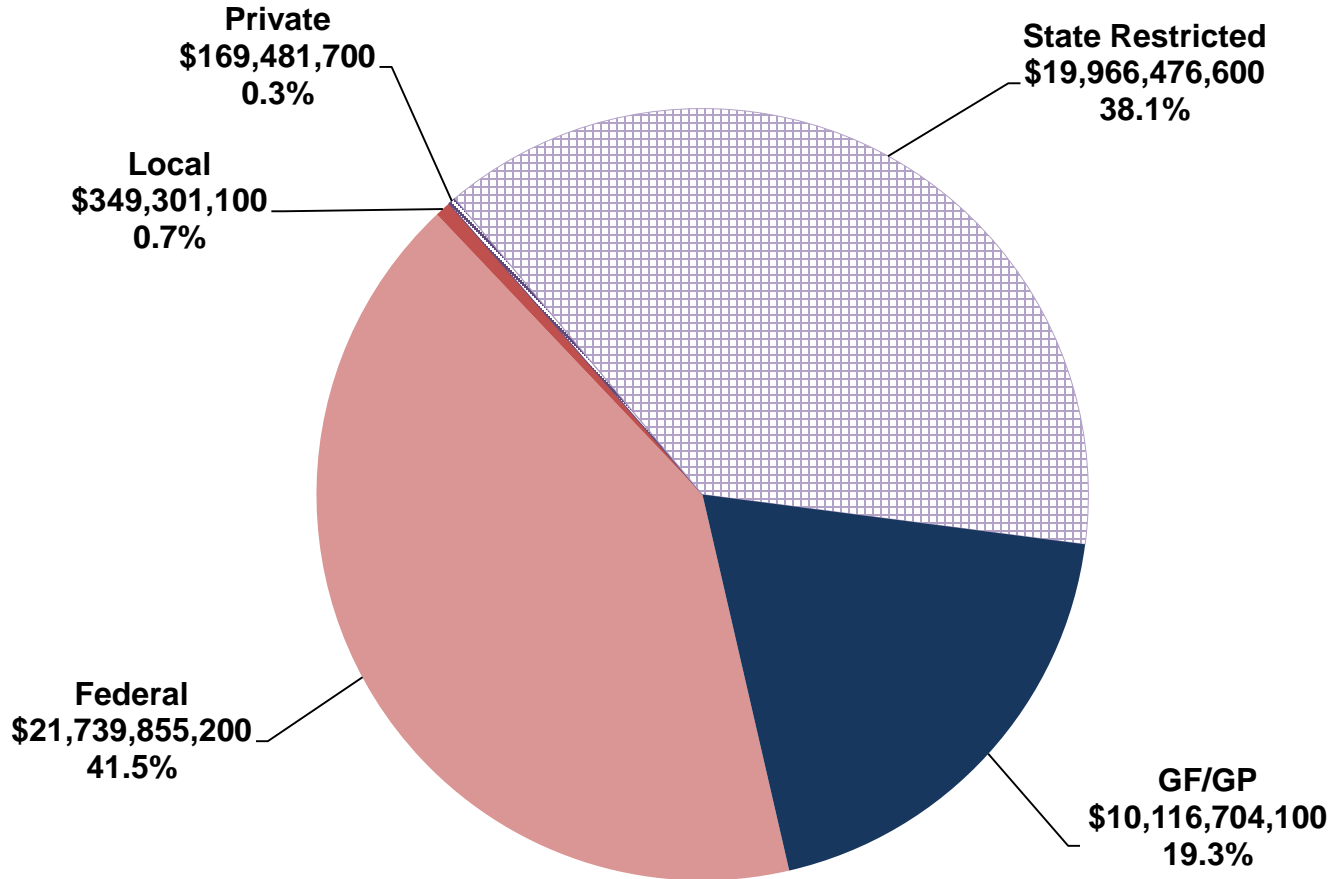
The total number of state employees has declined by about 15,000 (24%) since FY 2001.



CURRENT STATE BUDGET

FY 2014-15 State Budget by Source

About 80% of the \$52.3 billion state budget is funded by federal or restricted sources. State restricted sources can be either constitutional (for example, the School Aid Fund) or statutory in nature.



FY 2014-15 State Budget

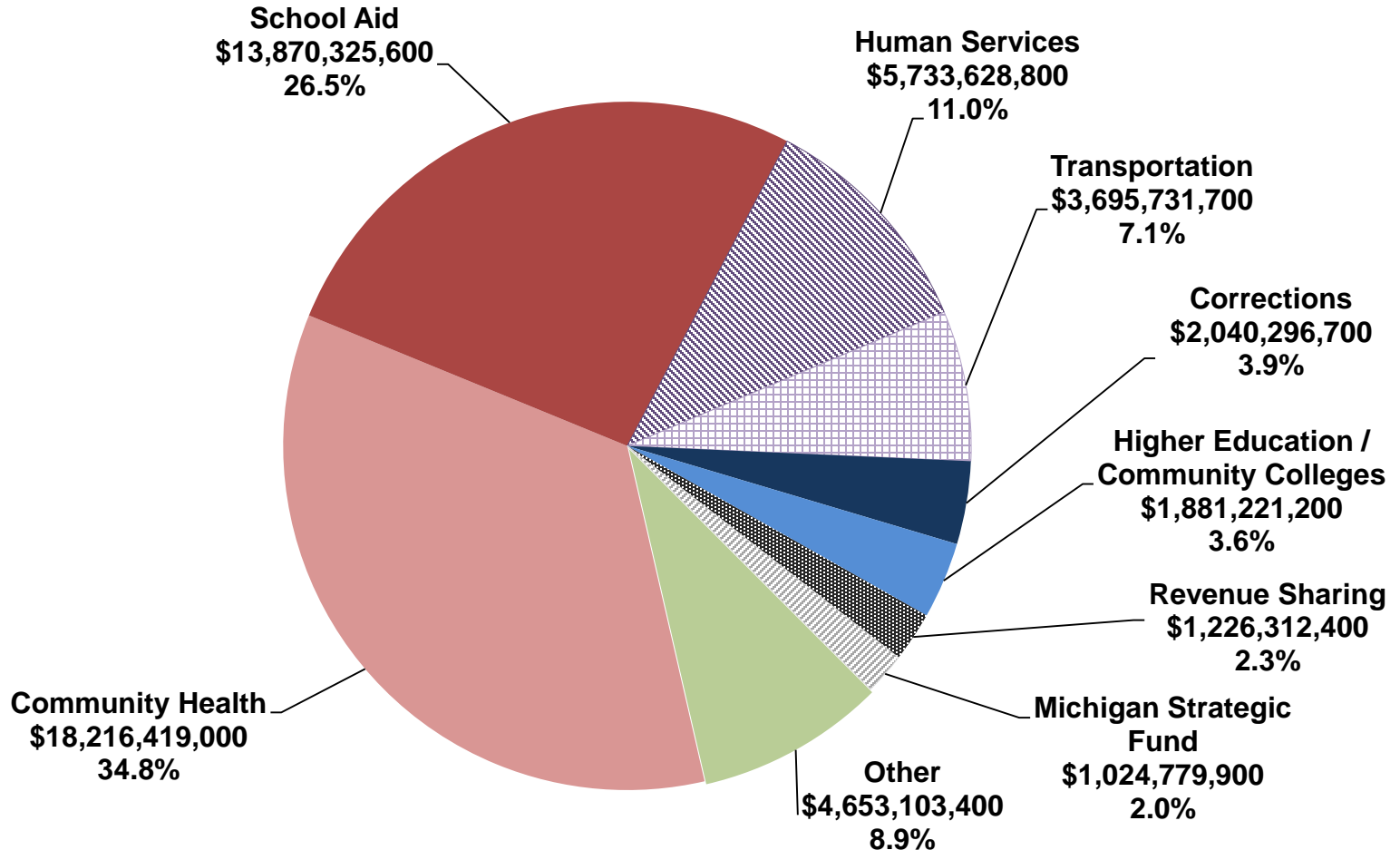
Millions of \$

Budget Area	Adjusted Gross	GF/GP
Community Health	\$18,216.4	\$3,239.7
School Aid	13,870.3	114.9
Human Services (Dept. of)	5,733.6	995.5
Transportation	3,695.7	284.6
Corrections	2,040.3	1,980.8
Higher Education	1,516.5	1,214.9
Treasury: Revenue Sharing	1,226.3	0.0
Treasury: Strategic Fund	1,024.8	244.6
State Police	645.8	414.2
Treasury: Operations	536.2	118.1
Licensing & Reg Affairs	528.0	40.0
Environmental Quality	493.1	40.9
Natural Resources	383.3	48.6
Community Colleges	364.7	167.1
DTMB: Operations	330.6	224.5

Budget Area	Adjusted Gross	GF/GP
Education (Dept. of)	\$287.1	\$82.1
Judiciary	285.4	186.5
DTMB: SBA Rent	254.6	254.6
State	204.0	17.5
Military & Veterans Affairs	166.8	49.2
Treasury: Debt Service	152.4	152.4
Legislature	131.9	127.4
Agriculture	84.1	45.9
Attorney General	66.0	38.3
Insurance & Fin Services	64.5	0.1
Legislative Auditor General	16.9	14.9
Civil Rights	16.4	13.4
Executive Office	5.9	5.9
TOTAL	\$52,341.8	\$10,116.7

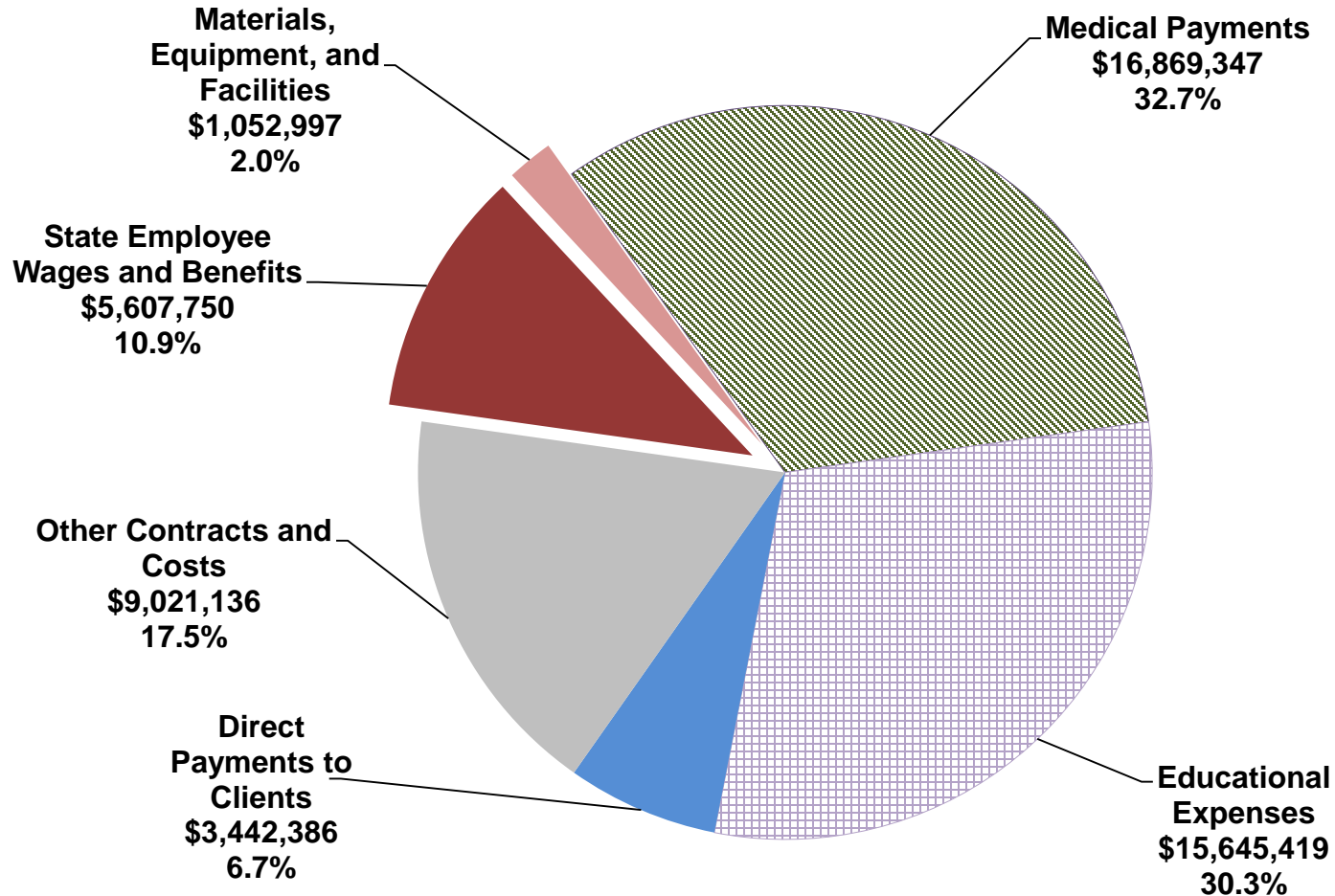
FY 2014-15 Adjusted Gross Appropriations

Large portions of the \$52.3 billion state budget consist of payments to health care providers, school districts, universities and colleges, and local units of government.



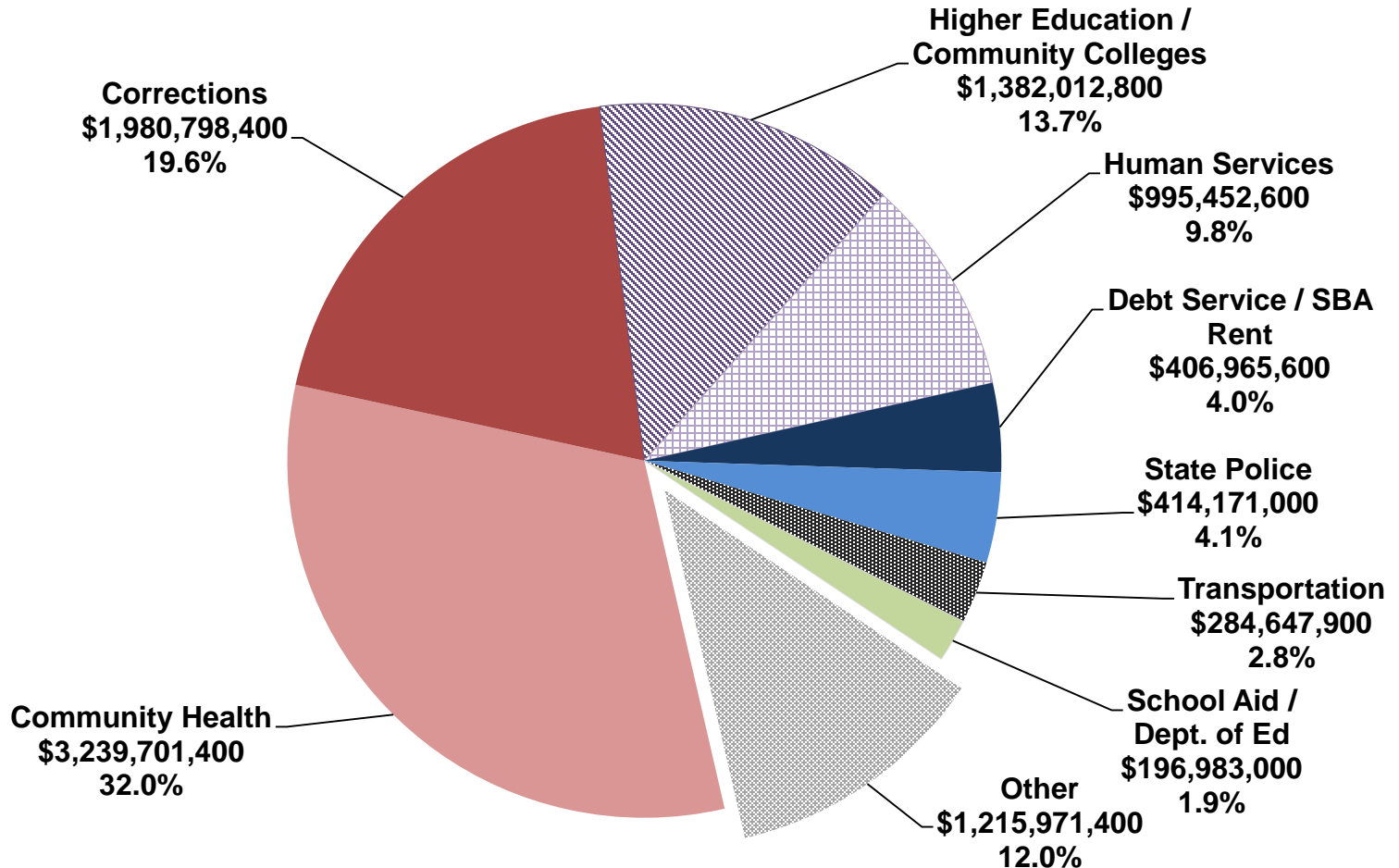
FY 2014-15 Statewide Spending Plan

Approximately 13% of the total planned expenditures of \$51.6 billion will support state employee wages/benefits and other costs of operating state government. The remaining 87% consists of payments to outside entities and individuals.



FY 2014-15 GF/GP Appropriations

88% of the \$10.1 billion GF/GP budget is appropriated for health and human services, public safety, education, debt service, and one-time Transportation purposes. The remaining 12% (\$1.2 billion) provides funding for 11 state departments, the Michigan Strategic Fund, and the Judiciary, Legislature, and Executive Office.



Major GF/GP Program Increases from FY 2011-12 to FY 2014-15

Funding Item	Millions of \$
Community Colleges: Operations	\$23.3
Community Colleges: Retirement Cost Reimbursement	52.3
Community Health/Corrections/Judiciary: Mental Health Initiatives	20.4
Community Health: Continue Primary Care Rate Increase (partial)	25.0
Higher Education: University Operations	132.7
State Police: New Troopers	41.5
MSF: Business Attraction & Community Revitalization (\$109.0 million total)	34.0
MSF: Community Ventures/Skilled Trades Training	19.8
MSF: Film Incentives (\$50.0 million total)	25.0
Revenue Sharing: Counties (GF/GP impact)	96.1
Revenue Sharing: Cities/Villages/Townships (GF/GP impact)	39.1
DTMB: Information Technology Development Projects (including public safety)	102.4
DTMB: Building Maintenance	28.0
Transportation: Federal Match	284.6
Treasury: Personal Property Tax Reform	20.8

Notes: (1) Includes funding amounts designated as one-time for FY 2014-15.

(2) Some items are full or partial restorations of FY 2011-12 reductions (Community Colleges/Higher Education/Revenue Sharing).

State Employee Compensation

FY 2014-15 Total: \$5.7 Billion (Estimated)

Roughly 50% of costs related to state employee compensation are funded by GF/GP revenue; remaining costs are funded by federal and restricted sources. Corrections employees account for roughly 50% of GF/GP compensation costs.

Salary and Wages: \$3.2 billion

- Average salary for a full-time state employee has increased from \$44,395 in FY 2002-03 to \$55,770 in FY 2012-13, which equates to growth of 2.3% per year.

Health Insurance: \$630 million

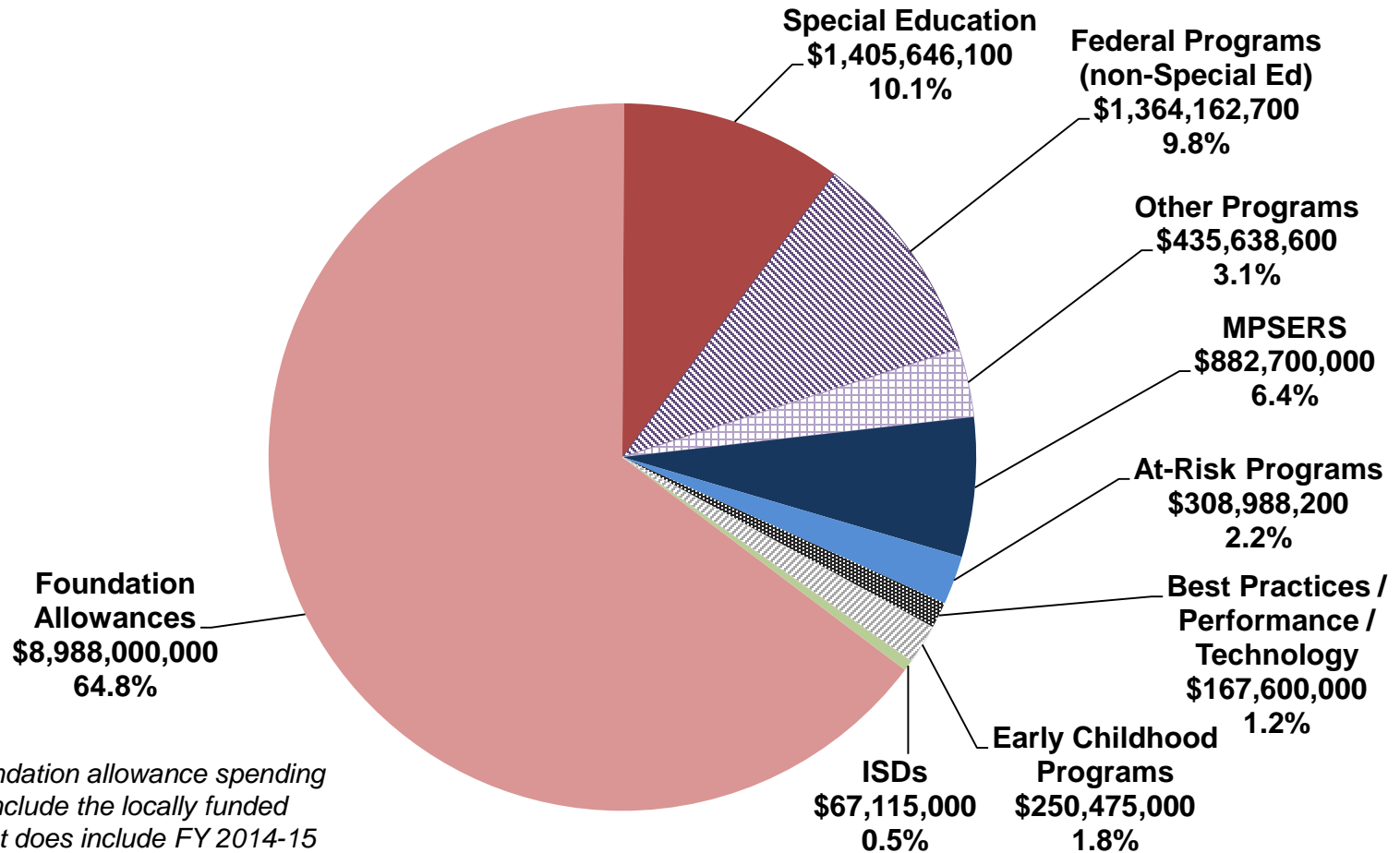
- Employee premium costs are paid on an 80/20 state/employee basis. Employee deductibles and copays have also been increased.

Retirement and Other Post Employment Benefits (OPEB): \$1.9 billion

- Costs have increased substantially in recent years due to unfunded liabilities created primarily by investment losses in 2008. Additionally, the Legislature's decision in 2011 to begin prefunding retiree health care benefits (OPEB) has resulted in short-term cost increases but reduced long-term liabilities.
- Employees hired since 1997 enter a defined contribution (DC, or 401k) retirement plan, rather than a pension plan. Employees in the pension plan now pay 4% of salary into the system. Employees hired since 2012 receive a DC cash benefit in place of retiree health care benefits.

FY 2014-15 School Aid Appropriations

Recent increases in the \$13.9 billion School Aid budget have been targeted based on specific requirements or purposes: retirement costs, early childhood, best practices, information technology.



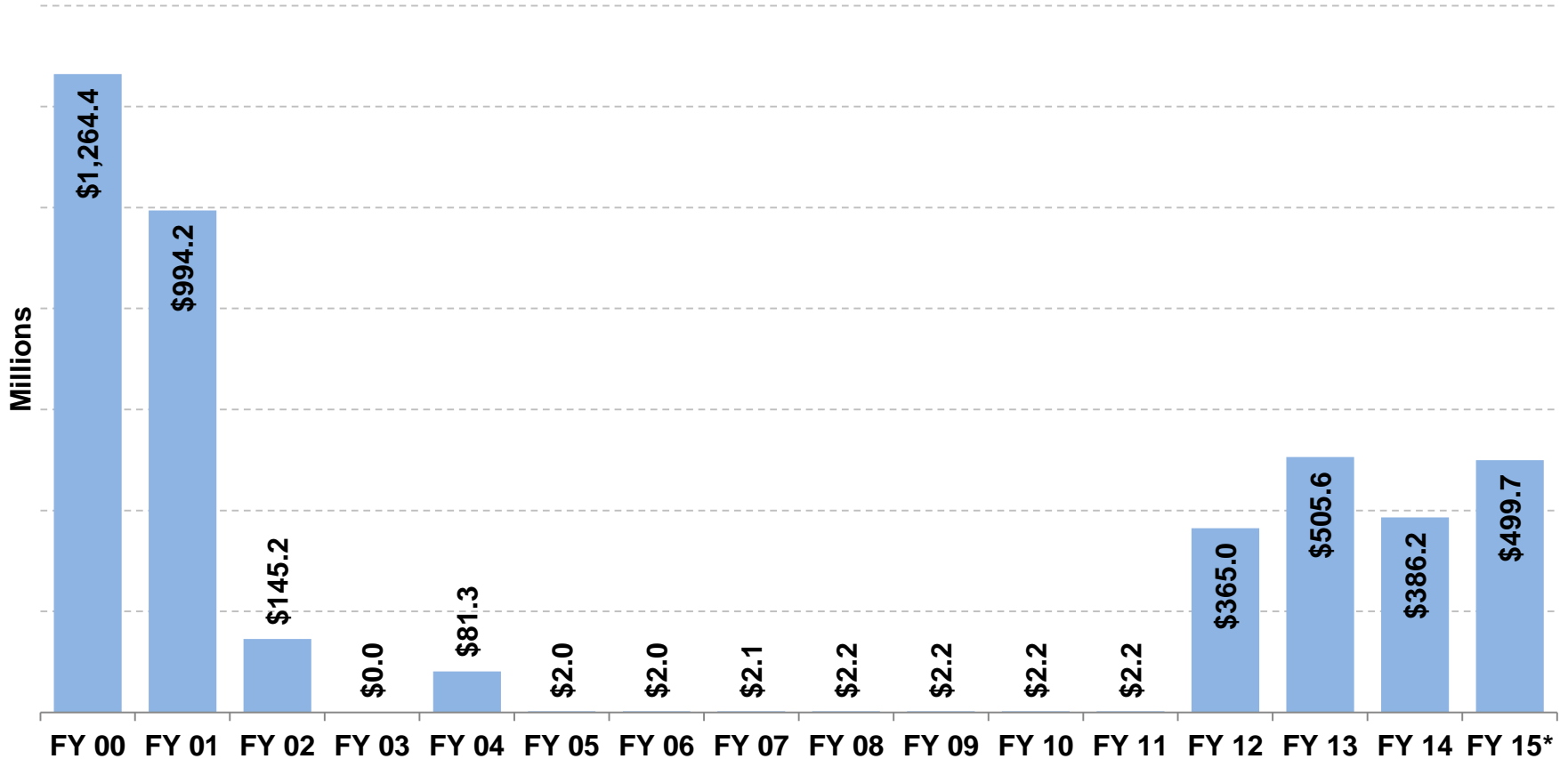
Note: Foundation allowance spending does not include the locally funded portion, but does include FY 2014-15 Equity Payment.

FY 2014-15 School Aid Budget

- **Foundation Allowance** – Provides an increase of \$50 per pupil to all districts.
- **Equity Payment** – Additional equity payment of up to \$125 per pupil for districts with foundation allowances below \$7,251.
- **MPERS Retirement Unfunded Liability Costs (State Share)** – Up from \$407 million in FY 2013-14 to \$675 million for FY 2014-15; allows for cap on unfunded liability rate charged to local districts and other employers.
- **MPERS One-time Additional Unfunded Liability Payment** – Additional \$108 million to pay down long term MPERS liabilities.
- **Early Childhood Increases** – Another \$65 million increase (more than doubling the program over last two years); adds another 15,000 half-day slots and dedicates \$10 million of the increase for preschool transportation.

Budget Stabilization Fund Balance

The large BSF balance accumulated during the 1990's was quickly depleted in the early 2000's. The balance has been partially restored in recent years, to about 2.3% of combined GF/GP and SAF annual revenue.



*HFA Estimate

Note: Reduction in balance for FY 2013-14 is due to state payment of \$195 million toward Detroit bankruptcy settlement; funds are to be repaid to BSF from state's share of tobacco settlement revenue over 20 years.

BUDGET OUTLOOK

Major General Fund Budget Pressures

- **Budget Shortfalls**
 - Estimated General Fund budget shortfall of \$454 million for FY 2014-15.
 - Ongoing General Fund revenue roughly \$200 million lower than baseline budget for FY 2015-16.
 - Resolution of FY 2014-15 shortfall will affect FY 2015-16 budget outlook.

- **Venture Michigan Fund**
 - Enacted into law in 2003; state tax vouchers utilized as collateral to raise capital that has been invested in multiple venture funds.
 - Anticipated revenue losses of \$50 million per year for FYs 2014-15 and 2015-16 and \$40 million for FY 2016-17 for first round of venture investments.

- **Personal Property Tax Reform**
 - All state losses/costs directed to General Fund.
 - Total projected costs of \$126 million for FY 2015-16, increasing to \$350 million in FY 2016-17 as larger personal property exemptions become effective.

- **Transportation**
 - \$285 million GF/GP appropriated for road projects in FY 2014-15 is classified as one-time.
 - May 2015 ballot proposal would increase Transportation revenue by about \$1.3 billion per year, as well as School Aid Fund revenue by \$300 million and Constitutional Revenue Sharing by \$95 million.

Major General Fund Budget Pressures

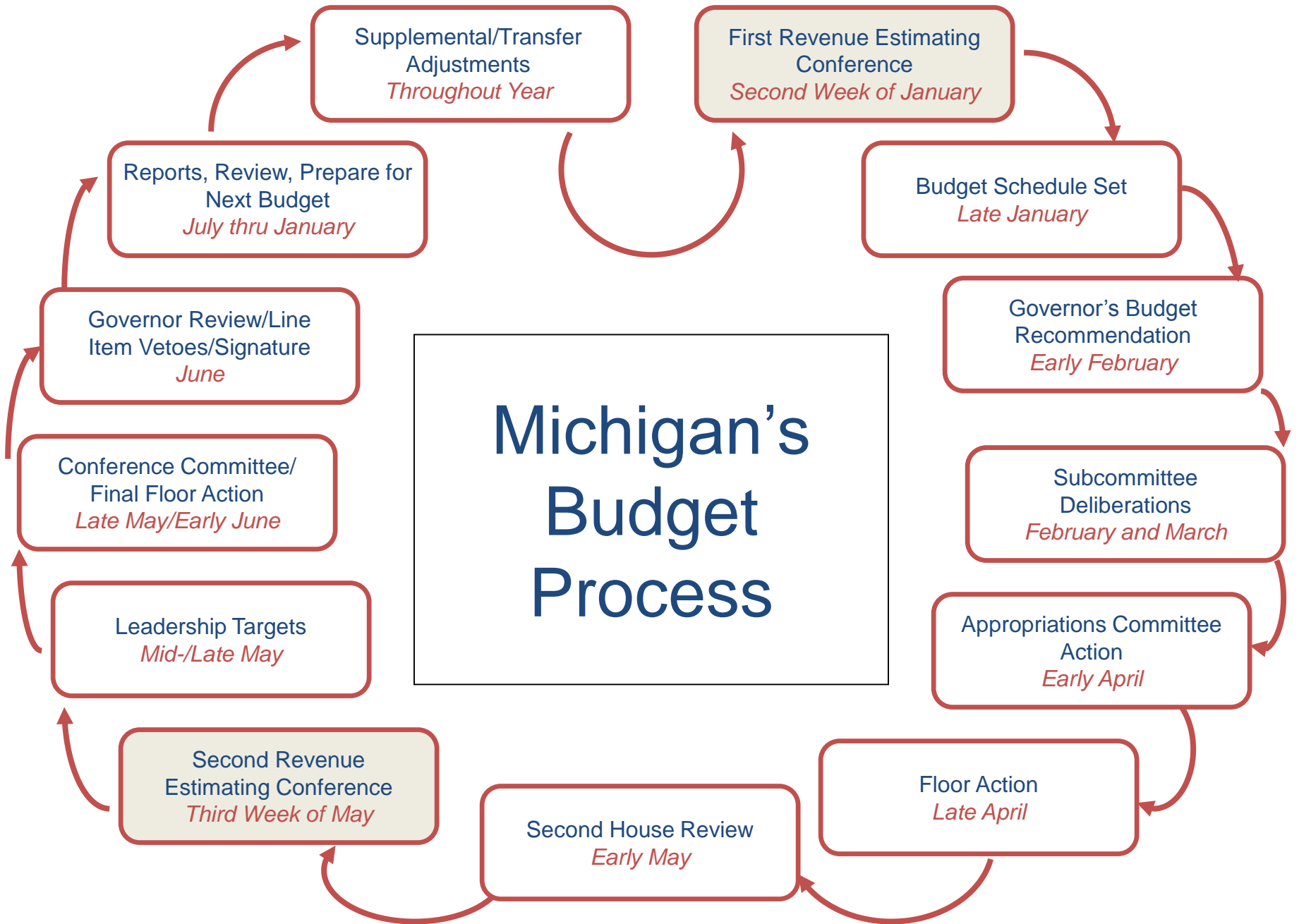
▪ **Medicaid Financing**

- Recent federal guidance indicates that state's Use Tax on Medicaid Managed Care Organizations (MCOs) must be discontinued by the end of 2016 (3/4 of FY 2016-17 affected).
- Automatic reversal of tax changes under current law (eliminate Use Tax on Medicaid MCOs, restore HICA rate from 0.75% to 1.0%) will leave General Fund budget hole of roughly \$150 million per year (also impacts SAF).
- Health Insurance Claims Assessment (HICA) sunsets at end of calendar year 2017; if assessment isn't extended, it would create an additional budget hole of \$300 million or more per year.

▪ **Medicaid Expansion Match Costs**

- Currently 100% federally funded; five percent match costs begin January 1, 2017, phasing up to ten percent match costs begin January 1, 2020.
- Projected costs of \$120 million GF/GP in FY 2016-17, increasing to between \$300 and \$350 million in FY 2020-21.
- Discontinuing expansion and shifting mental health and other costs back to state would cost roughly \$300 million per year.
- Expanded Medicaid program under Healthy Michigan Plan sunsets when/if costs to state outweigh savings.

BUDGET PROCESS



House Fiscal Agency Budget Roles

- **Analytical**
 - Prepare budget documents providing both summary-level and detailed information on proposed budget changes under Executive Budget and subsequent legislative versions
 - Gather objective information and analyze data related to specific budget issues of interest to legislators
 - Assist in development of alternative budget proposals; facilitate legislative decision making
 - Provide analyses of non-appropriations bills, including estimated fiscal impacts on state and local governments
- **Procedural**
 - Post meeting notices; clerk subcommittee meetings; prepare meeting agendas/minutes
- **Technical**
 - Prepare substitute appropriation bills based on legislative decision making
 - Prepare amendments proposed during subcommittee, committee, and floor debate
 - Prepare supplemental appropriations bills and legislative transfer documents (as well as associated summaries/explanations)
- **All tasks are completed in compliance with statutory requirements for nonpartisanship and confidentiality.**

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