Michigan League for Human Services

April 2009

FY2010 State Budget Update

The FY2010 Executive Budget, released in February just days before passage of the federal American Recovery and Reinvestment Act (ARRA), included very little stimulus funding in part because the bill had not been passed, and in part because the governor indicated she did not want to use stimulus funding for ongoing programs. The Executive Budget included a mix of revenue enhancements and program reductions with only $500 million of stimulus funding related to Medicaid to close the then-projected shortfall of $1.4 billion for FY2010. In addition, the budget assumed the use of just over $300 million in FY2009 to close the January projected shortfall of $312 million for the current year.

There was an expectation that an Executive Budget revision would be proposed to reflect additional stimulus funding contained in the ARRA and mitigate the need for the reductions proposed in the Executive Budget. As the maintenance of effort provisions of the ARRA for health and education became clear, and Michigan's revenues continued to decline from the level agreed upon in the January 2009 Revenue Estimating Conference, it became less clear what courses of action would be pursued by the Governor and the Legislature. Initially, both indicated the intention to not use the stimulus funding for ongoing program funding. However, the maintenance of effort requirements for federal education funding specify that formula funding cannot be reduced, which requires the Governor's recommended per-pupil reduction of $59 to be reversed. It was also clear from initial stimulus proposals that Medicaid eligibility reductions would not be allowed if a state wanted to take advantage of the increase in federal matching funds for Medicaid. The Governor recommended no Medicaid eligibility reductions; the federal funding increase for Michigan is projected to total more than $2.2 billion over fiscal years 2009, 2010, and the first quarter of 2011.

With the dramatic drop in revenues for the first three months of this year and the auto industry teetering on the brink of bankruptcy, the budget process has hit a bump in the road. The governor recently stated that even if all of the available federal stimulus funds were used to shore up the budget, "deep spending cuts would still be needed to bring the budget into balance" in the current year. A revised revenue estimate for FY2010 is not scheduled to be released until mid-May; however, legislative leadership and the Governor began joint revenue discussions in mid-April. Those discussions led to the acknowledgment of a currently projected $750 - $800 million shortfall for fiscal year 2009, the fiscal year that ends on September 30, 2009. Revised projections for FY2010 have not been released and may not be before the official Revenue Estimating Conference on May 15th.

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Following the recent assessment that revenues could be as much as $800 million short in the current year, the governor indicated she would propose an Executive Order to reduce spending and solve some of the problem with additional stimulus funding. It is not clear if the governor intends to present a revised recommendation for FY2010.

While the resistance to using stimulus funding to fill budget shortfalls has been very strong to date, particularly in the Senate, where leadership has called for resolving budget shortfalls with cuts and continues to call for a cuts-only approach, mounting deficits could be large enough to preclude the ability to achieve the magnitude of savings that would be required during the remainder of the fiscal year. With the revenue picture for FY2009 turning so bleak, it is not clear how large the shortfall for FY2010 will become. Also it is important to recall that the FY2010 Executive Budget recommendation closed a $1.4 billion shortfall primarily caused by declining revenues only a few months ago.

In the human services (excluding Corrections) and education budgets, recommendations to date from the House have added significant increases financed with stimulus funding, while the Senate has generally recommended additional reductions beyond those adopted from the Executive Budget. Although several bills had made it through the first chamber before the Easter break, when it became obvious that revenues were lagging so far behind projections, Senate leadership halted passage of further Department budgets before the Easter recess.

The Legislature reconvened the week of April 20 to the news of the acknowledged current-year shortfall. Both chambers are currently working on proposals to bring the current year budget into balance. No details have been released as of this writing. During that week, the House did complete work on the Department of Community Health budget, passing the bill recommended by the full Appropriations Committee.

The League supports a reasoned approach to this crisis and does not believe that further cuts, resulting in continued disinvestments in Michigan's residents, are the right solution. Over the last several years, more than $4 billion have been cut from the state budget, and the impacts are being felt throughout the state from the crumbling roads and infrastructure to the shredded safety net (see Walking a Tightrope Without a Net). It is also important to consider the economic benefit of state services and spending during a severe economic downturn. Mark Zandi of Moody's Economy.com estimates that for every dollar of federal stimulus funding used to avert state budget cuts, $1.38 of economic activity results.

As a resolution to the FY2007 budget crisis, when the state was faced with a similar situation, the Legislature chose to raise taxes, but only on a temporary basis, and not in a manner that generated growth for the future. The structural deficit was clearly not fully addressed then and so remains unresolved. The League supports comprehensive tax reform and restructuring to generate adequate, stable and fair revenues to meet the needs of our residents and businesses.

One component of comprehensive tax reform should include a critical review of Michigan's tax expenditures (special tax policies that benefit only certain industries, groups, or activities) which now total more than $35 billion annually. Many of these tax policies have been in place for years with no review to determine if they are achieving their stated purposes. The League recommends an annual review of the tax expenditures by the appropriations committee as part of the budget process (Tax Expenditures: Silently Draining the State Budget) . A 1 percent reduction in tax expenditures would generate $350 million that could provide needed state services to the thousands of struggling residents. Numerous other revenue options are available to state policymakers, including a graduated income tax and an expansion of the sales tax to services, to avert devastating state budget cuts if they choose to pursue them.

Further information on the budget process will be provided as detailed proposals are released.