Michigan League for Human Services

Facts Matter

Facts Matter is a series of briefs highlighting Michigan's budget and tax system

Michigan's Deficit:

- Current year General Fund deficit of $1.8 billion addressed with $1.1 billion stimulus dollars and $708 million in cuts
- Projected to be $1.8 billion for General Fund and School Aid in FY2011
- Michigan has cut more than $4 billion this decade

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The Budget Deficit: It's Not Just the Economy

There are two kinds of deficits, structural and cyclical. Michigan has both:

1. A cyclical deficit is one that is driven by the economy and business cycle, and goes away in good economic times.
2. A structural deficit exists regardless of the economy—during good times and bad times. It occurs because the state's revenue structure does not bring in enough money to fund services and programs. Because it is structural in nature, it can only be solved by structural changes.

The size of Michigan's deficit

- Fiscal year 2010 marks the 10th consecutive year that state revenues have not been adequate to fund state services and programs.
- The current year's deficit is being addressed with $1.8 billion in federal stimulus dollars and over $708 million in cuts.
- Projections indicate the state faces an estimated shortfall of $1.8 billion for fiscal year 2011.
- Since the first decline in revenues in fiscal year 2001, Michigan has experienced cumulative deficits well in excess of $10 billion, has exhausted over $6 billion in fiscal reserves and has instituted over $4 billion in spending cuts.

The response so far

Over the years, in response to the ongoing structural deficit, the Michigan Legislature cut the budget, raised the income tax temporarily and used other one-time measures. None of these is an acceptable long-term solution. Spending cuts to public safety, health care, human services and education are being felt all across the state. Not only do spending cuts cripple services, but they are also bad for the economy, as they lead to a further loss of jobs. Given the size of the current deficit and the implications, it is virtually impossible to address the deficit solely through cuts.

While the temporary income tax increase is helping to generate additional revenues for the state; it is only temporary and is declining as large numbers of workers lose jobs. The rate will begin to decline starting in October 2011 and will return to 3.9 percent on October 1, 2015. This will result in a further reduction of state revenues.

Since 2001, Michigan has undertaken a combination of one-time measures, spending reductions and modest revenue enhancements to balance each year's budget. These have not addressed the structural deficit, which is a serious and growing problem. It is time for state policymakers to look at revenue options that will provide long-term solutions.

Better options for addressing the structural deficit

- Extend the 6 percent sales tax to a limited number of services. (Excludes medical, nonprofit and business-to-business services together valued at over $9 billion.)
  Projected Revenue: $1.65 billion

- Institute a graduated income tax. One scenario would reduce the tax burden of more than 90 percent of Michigan filers with a tax liability. The resulting revenue could be expected to grow more rapidly than is the case with the existing flat income tax.
  Projected Revenue: $600 million

- Reduce senior tax preferences to a level equal to Kentucky, the second-most generous senior preference state (Michigan is currently No. 1, by over 27 percent).
  Projected Revenue: $200 million

- Increase the beer tax, which was last adjusted (reduced) in 1966, from 2 cents to 6 cents per 12 ounces. (The proposal would restore two-thirds of the erosion in the purchasing power of beer tax revenues since 1966, due to inflation.)
  Projected Revenue: Almost $90 million

- Decouple from the phase-out of the Federal Estate Tax to permit the state to again receive a portion of the taxes paid by Michigan estates.
  Projected Revenue: $250 million

- Repeal a series of tax expenditures that have, in previous legislative sessions, been approved for elimination by one house or the other, or recommended for repeal by the governor.
  Projected Revenue: $400 million

- Reduce the incarceration rate and average cost per prisoner differentials between Michigan and the other Great Lakes states by 50 percent. While not a revenue enhancement, this recommendation would free up resources for use in resolving anticipated shortfalls.
  Spending Reduction: $300 million

Note: Revenue and spending projections are annual