Michigan League for Human Services

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Keeping the Lights on in Michigan

How a Federal Stimulus Package and Smart State Choices Will Help

Recessions create tenuous times for states. As revenues are declining, demand for safety net programs is increasing, creating difficult budget tensions between balancing needs with available revenues. Because of the depth and projected length of the current recession, congressional leaders and the new administration are actively discussing a second stimulus package to boost the economy and provide fiscal relief to state governments.

As policymakers at the federal and state levels separately debate the best course of action to stimulate economic activity and maintain public services in the states, it is critical that they pass legislation and implement complementary, not counterproductive, policies at the state and federal levels. The laws governing federal and state budget actions are neither compatible nor consistent: States are required to balance their budgets annually, while the federal government operates without such a requirement and can operate in deficit. This explains the ability of the federal government to provide a major stimulus package during a recession. While there is not agreement on the size of the stimulus package, economists agree that it is both the right thing to do and necessary in view of the depth and projected length of the current recession.

As federal policymakers are discussing the size and components of a second federal economic recovery package to generate spending and provide fiscal relief to states, state policymakers across the country are discussing and enacting state spending cuts in response to declining state revenues. In Michigan, Governor Granholm has issued an Executive Order to reduce state spending to bring it more in line with projected revenues. While she indicated she would not recommend deep budget cuts with a sizable federal aid package under discussion, she did propose a significant cut, $23 million, in the Family Independence Program, the key safety net cash assistance program for very low-income families. This reduction resulted from fewer families than budgeted receiving cash assistance, an alarming fact in the current economic climate in Michigan.

Federal Stimulus Options:

At the federal level, lawmakers are discussing several targeted areas for the federal economic recovery package. Among the areas under discussion are:

- Food assistance benefit increases through the Supplemental Nutrition Assistance Program (SNAP), formerly the Food Stamp Program;
- Increases in the federal share of Medicaid payments (known as the Federal Medical Assistance Percentage, FMAP);

- Extension and broadening of Unemployment Benefits;
- Block grants to states to provide fiscal relief;
- Increases in funding for immediate action on infrastructure projects.

The proposed increase in food assistance benefits is a tremendous stimulus from a state perspective. The Supplemental Nutrition Assistance Program is funded 100 percent by the federal government, requires no state contribution, and the benefits go directly into the state's economy as beneficiaries use their increases to purchase food. This proposal would be particularly beneficial to Michigan's economy as SNAP beneficiaries continue to increase, reaching new record highs every month.

An increase in the Federal Medical Assistance Percentage for Medicaid is also a very effective economic stimulus for states, as payments to health care providers generate significant economic activity, while Medicaid recipients continue to receive needed health care services. Since Medicaid is a jointly funded program between the state and federal governments, states must continue to provide a share of the cost. The stimulus package, proposed but not passed by the Senate, included an eight percentage point FMAP increase which would have correspondingly reduced the state share of payments by eight percentage points. In Michigan, the FY2009 federal matching rate for Medicaid is about 60 percent, with the state contributing the remaining 40 percent of Medicaid expenditures. An increase to 68 percent in federal matching funds would reduce the state contribution to 32 percent. Therefore, for every $100 of Medicaid spending, the federal government would provide $68, while the state would contribute $32. An eight percentage point increase in the Medicaid matching rate would provide about $800 million in annual benefits to the state.

Conversely, if the state reduces funding for Medicaid, for every $100 of state funding reduction, at the enhanced rate, nearly $315 of health care services would be lost, as would be the economic activity that would have been generated. Several states, due to the severity of their budget deficits, have already announced reductions/limitations in their Medicaid programs to save state funds. To date, Michigan has preserved its Medicaid program, and recent statements by the governor indicate she does not intend to recommend Medicaid cuts.

Infrastructure projects continue on Michigan's "to do" list as road conditions deteriorate due to lack of state funding to match available federal funds. Department of Transportation officials recently testified that if Michigan is not able to match federal transportation funds, the federal funds will be allocated to other states. It is not clear what level of state funding might be required in a stimulus package. Funding for planned, but not yet initiated, municipal infrastructure projects is also under discussion for inclusion in the stimulus package.

In addition to federal fiscal relief, states have numerous options to avoid or reduce the need for damaging budget cuts. Revenue increases at the state level, to sustain public spending, are seen by many economists as not only preferable, but as yielding better outcomes than budget cuts.

State Options to Increase Revenue:

There are numerous actions, short of a comprehensive overhaul of the tax structure, that could be enacted quickly to increase revenues and avert program reductions that will diminish the quality of life in this state. Opportunities include:

- Immediately decouple from the federal estate tax policy, and re-establish the estate tax in Michigan, increasing revenues by about $250 million per year;
- Review tax expenditures (special tax policies that benefit only certain industries, groups, or activities) to determine if the purpose for which they were originally passed is still being served and eliminate those that are no longer

serving their intended purposes. The total value of tax expenditures currently exceeds $35 billion in foregone state revenue. A **one percent** reduction in tax expenditures would provide $350 million per year in revenue to the state's coffers;

- Increase the beer tax, not increased since 1962, by $.02/can to generate about $43 million;
- Increase the wine tax, not increased since 1981, by doubling the per gallon tax to $1.02, to generate about $8 million in new revenue.

As policymakers deliberate options, particularly reductions in state services, during this recession, it is important to weigh the impact of program cuts on Michigan's economy, its most vulnerable residents, and the quality of life in this state, and whether as a state, we can afford further cuts. Policymakers must ask the following questions:

- Would more uninsured residents and more uncompensated health care benefit the state and medical providers?
- Would larger class sizes enhance students' learning and opportunities for success?
- Are too few families being priced out of the opportunity for higher education for their children?
- Would further deterioration and less maintenance of our roads be beneficial and attract new business, particularly during the winter season?
- Would reduced air and water quality and more pollution be good for residents or attract more businesses to the state?

If the answers to the above questions are "no," then Michigan does not have a spending problem as some assert, rather it has a revenue problem. If state revenues had not declined for FY2009, Michigan would not have a significant budget shortfall. Michigan has a current and ongoing revenue problem, and that is what must be addressed.

mar/EconStimulus II