Michigan League FOR Human Services

June 1, 2007

State Budget Update: Deficits Not Fully Resolved

Legislature Approves Sale of Tobacco Settlement Bonds and Withdrawals from other Restricted Revenues to Close FY2007 Budget Deficit; FY2008 Budget and Single Business Tax Replacement Negotiations Continue

On May 30th, after months of debate regarding how to resolve a mounting state deficit, the Michigan House and Senate voted to effectively dodge the issue for yet another year by selling approximately $400 million in bonds secured by future tobacco settlement revenues, drawing down balances in several restricted funds, and implementing program reductions that address a small percentage of Michigan's out-year structural deficit. The following table reflects the major components of a tentative House/Senate agreement intended to resolve a deficit of approximately $800 million for the current fiscal year ending September 30th.

One-Time Asset Sales, Accounting Adjustments, Payment Delays and Restricted Fund Withdrawals	
1. Securitize Future Tobacco Settlement Payments	$406.8 MIL
2. Withdrawal from the Refined Petroleum Environmental Remediation Fund	70 MIL
3. Withdrawal from the Higher Education Student Loan Fund (estimate)	90 MIL
4. Withdrawal from the State Campaign Fund	7.2 MIL
5. Withdrawal from the Convention Facilities Upgrade Fund	35 MIL
6. Withdrawal from Uncommitted 21st Century Funding	30 MIL
7. Withdrawal from Comprehensive Transportation Fund (Soo Locks set-aside funds)	5.3 MIL
8. Withdrawal from the Michigan Conservation Corps Endowment Fund	20 MIL
9. Withdrawal from Department of Labor and Economic Growth Fund Balances	.5 MIL
10. Defer Current-year University and Community College Funding into FY2008	69.4 MIL
Subtotal	**$734.2 MIL**
FY2007 Program Reductions	
1. Higher Education Funding Reductions	$25.9 MIL
2. Arts and Culture Grant Reductions	3.6 MIL
3. Healthy Michigan Fund Reductions	3.2 MIL
Subtotal	**$32.7 MIL**
Other Unspecified Adjustments and Program Reductions	**$33.1 MIL**
Total One-time Adjustments and Program Reductions	**$800 MIL**

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Despite the Governor's indication that failure to address the current-year deficit through an increase in state revenues by June 1st would force her to reduce the K-12 Foundation Allowance by approximately $122 per pupil, reduce Medicaid provider reimbursement rates by 6 percent, and institute state employee lay-offs, she is expected to approve the finalized legislative agreement and suspend her reduction plans

While those at risk of cuts under the Governor's announced plan may be breathing a sigh of relief, it is recognized that the tentative solution to the state's FY2007 budget deficit will significantly exacerbate what had been identified as a $1.5 billion deficit in FY2008, raising the shortfall for the fiscal year beginning October 1st to approximately $2 billion — equivalent to 40 percent of funding for state programs that could be classified as "discretionary spending" under the broadest of definitions. While recent reports suggest that the legislature may approve tax and fee increases that would address as much as $1.5 billion of this anticipated shortfall, governmental reforms and additional program budget cuts will undoubtedly be on the table as FY2008 budget negotiations continue. It should also be noted that, even if the full FY2008 deficit is covered with revenue increases and program reductions/reforms, Michigan's structural deficit — driven in large measure by health care and Department of Corrections costs that are likely to continue to outpace revenue growth, will likely amount to several hundred million dollars per year for the foreseeable future.

On a potentially brighter note, negotiations related to a permanent replacement of the Single Business Tax scheduled for elimination on January 1st appear to be progressing toward a resolution that could be revenue neutral — a stated goal of the administration. While this outcome is not a certainty, the Michigan Chamber of Commerce has indicated publicly that revenue neutrality, while not as desirable as a net business tax reduction, is not an outcome that organization would oppose. Even this potentially positive news, however, must be tempered by the realization that the probable components of a finalized agreement will rely heavily on a corporate income tax that may prove to be a far less stable revenue source than the Single Business Tax it is designed to replace.

As more details regarding the budget and revenue issues discussed above become known, the Michigan League for Human Services will provide updates.

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