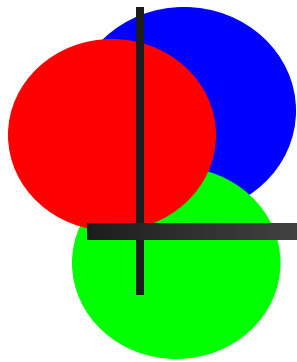


A Problem 10 Years in the Making



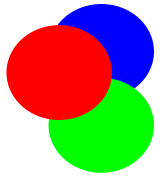
Prepared for:

**Representative Joan Bauer
District 68 Budget Town Hall**

April 21, 2011

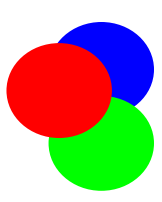


Mitchell E. Bean, Director



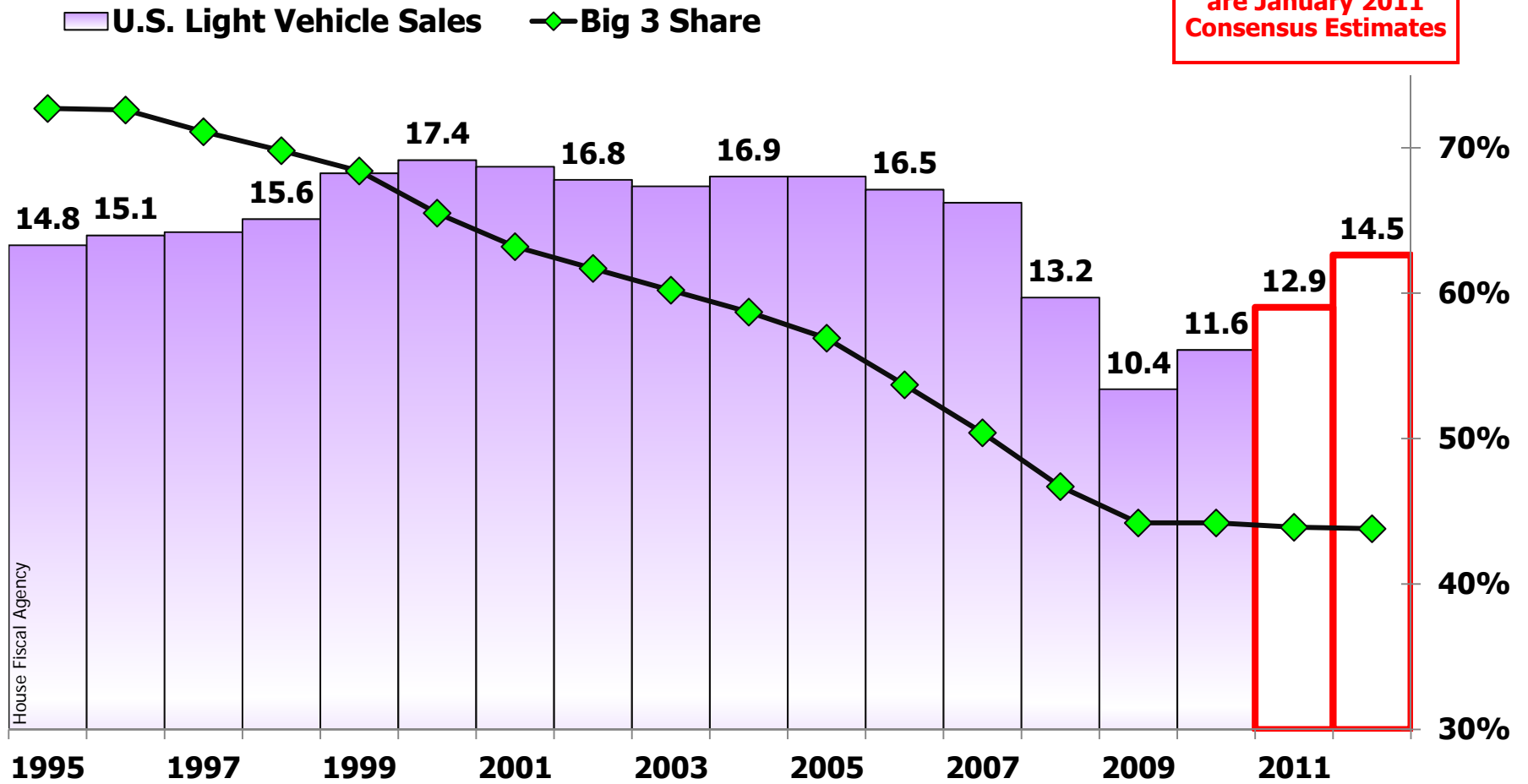
State Budget Shortfalls Caused By

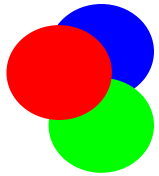
- **Severe economic contraction led by domestic auto industry**
- **State tax policy**
- **Increasing cost of Medicaid and corrections**
- **Chronic use of one-time fixes**



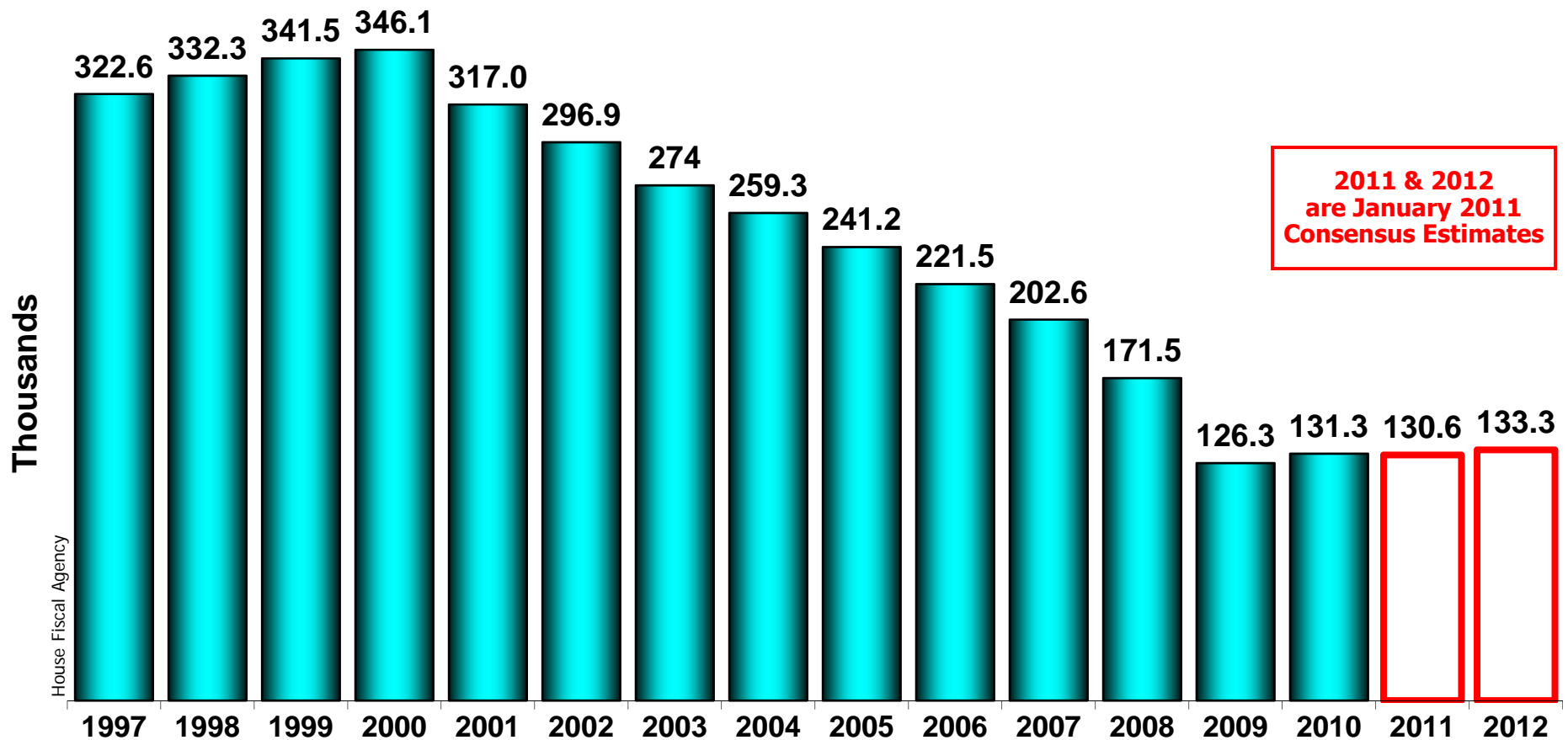
Big 3 Losing Market Share

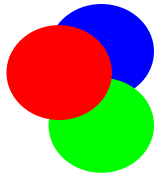
2011, & 2012
are January 2011
Consensus Estimates



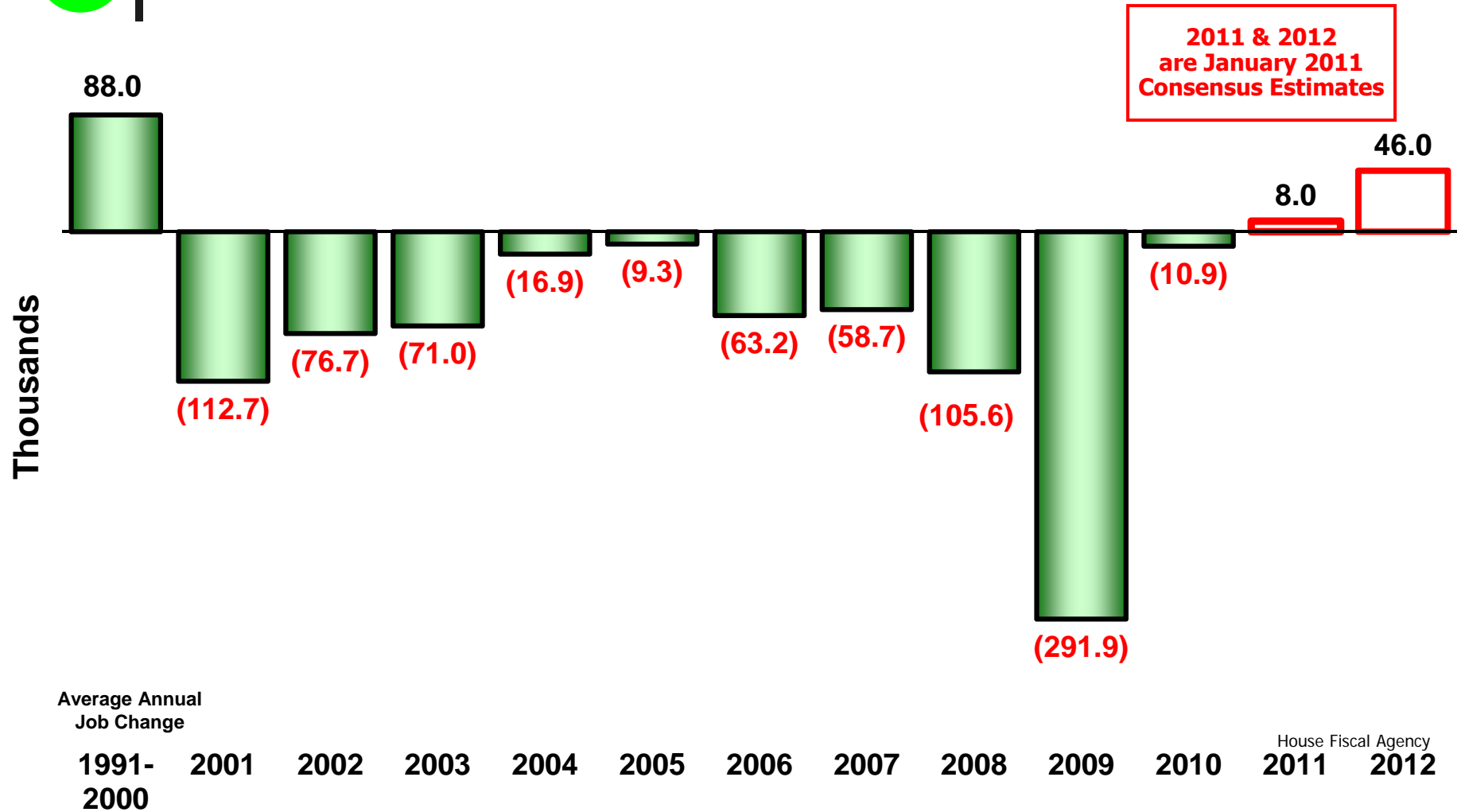


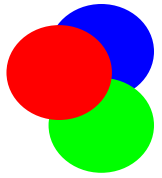
Michigan Vehicle Employment



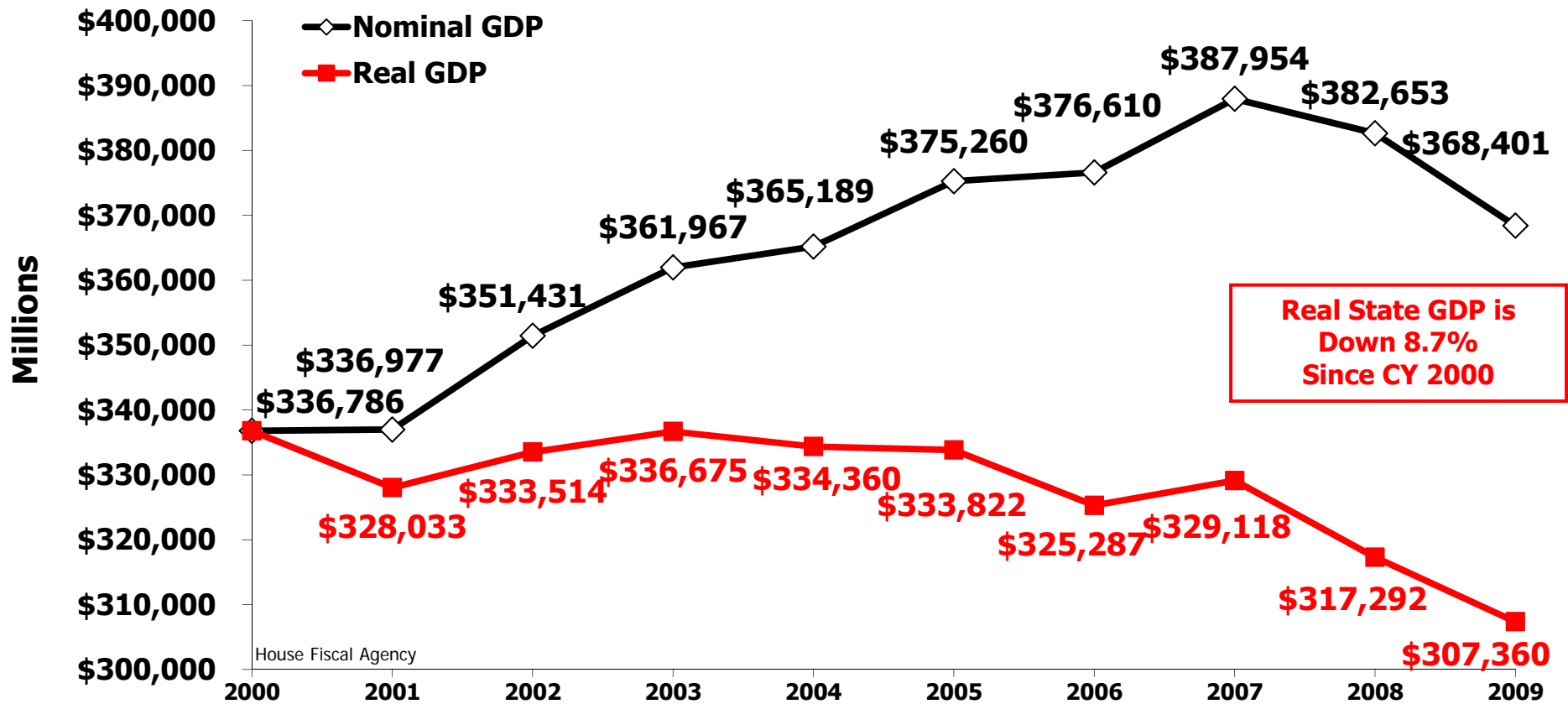


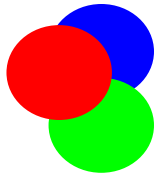
Job Change in Michigan



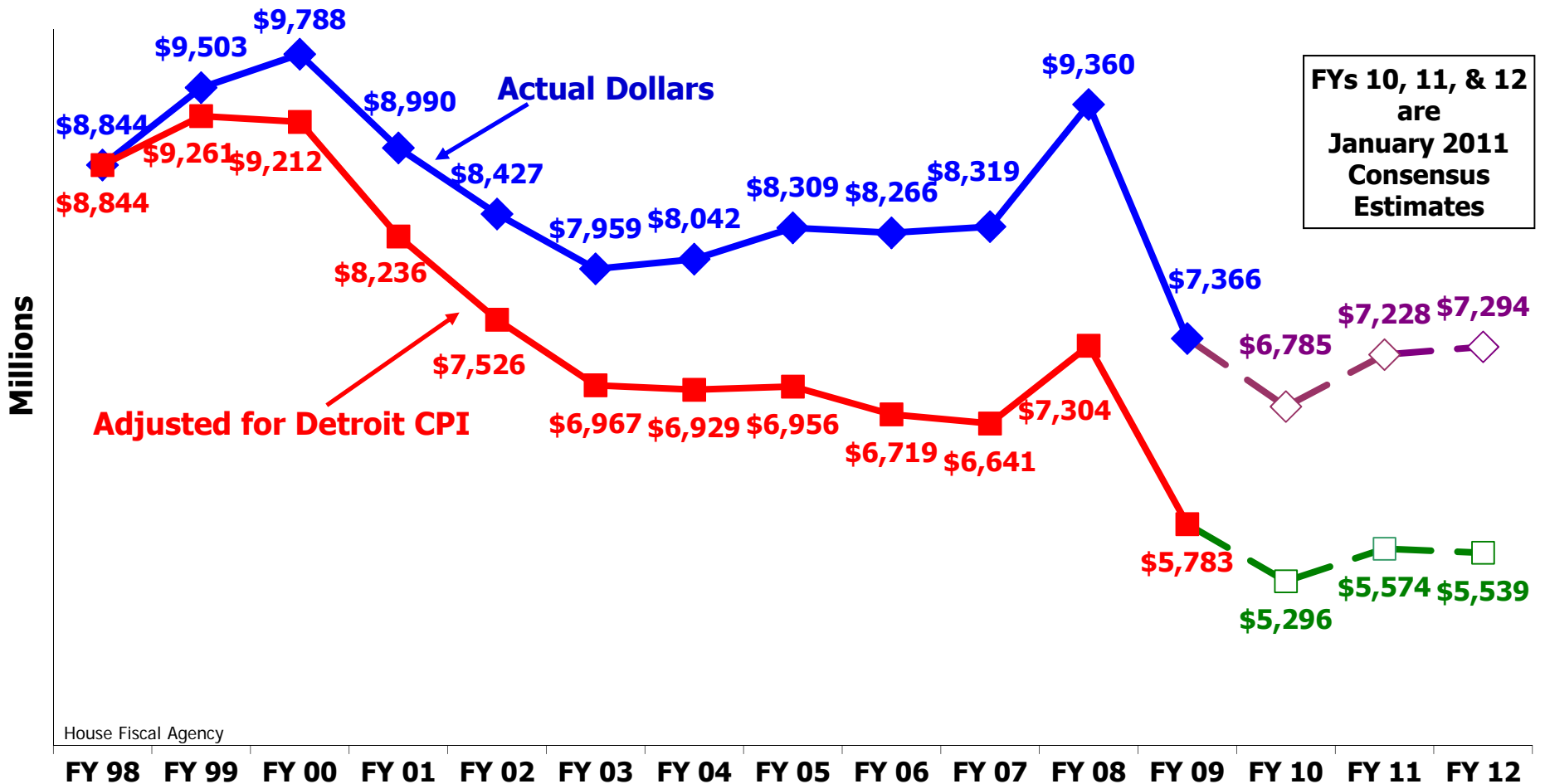


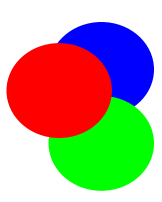
Real and Nominal State GDP



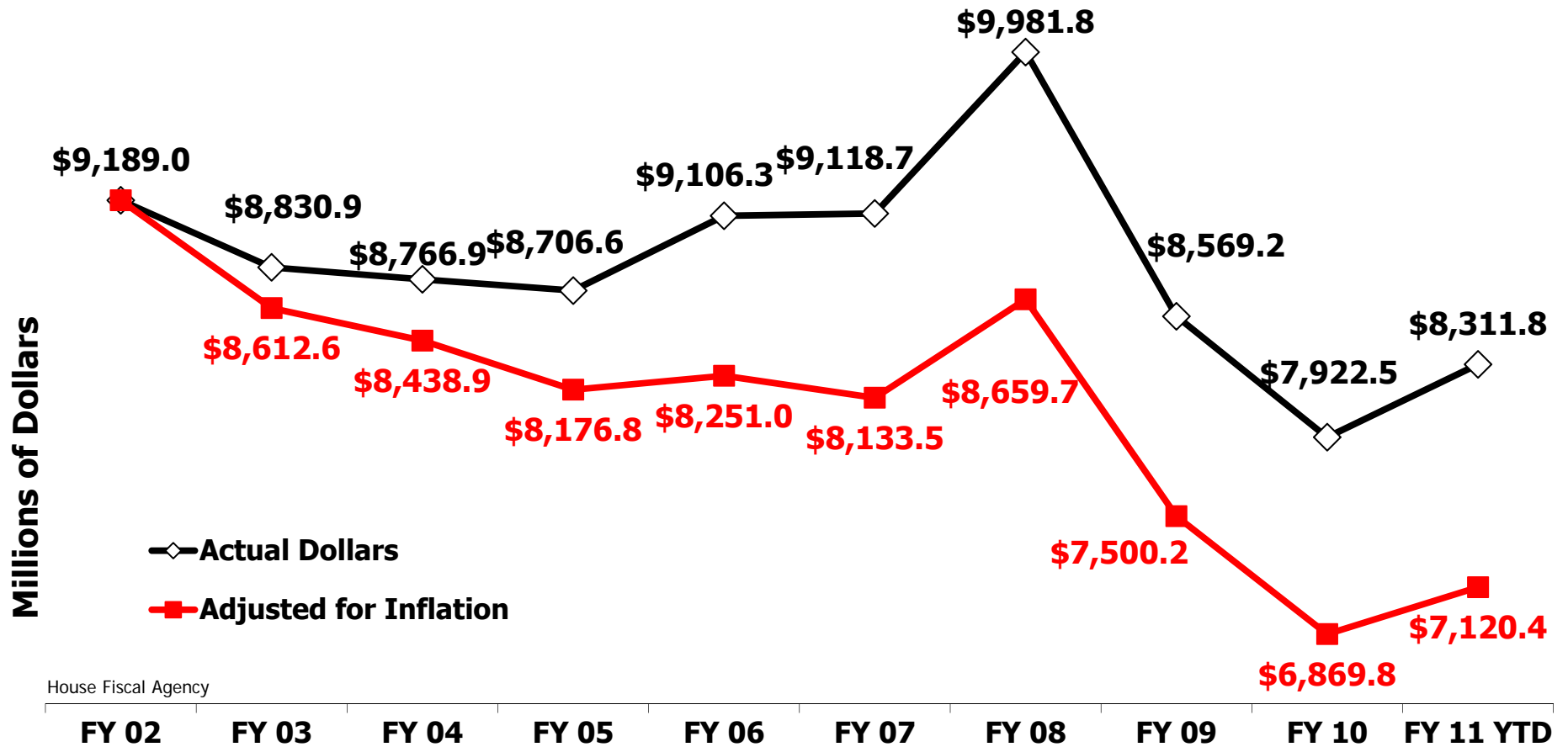


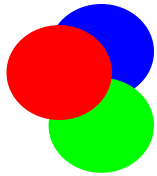
Inflation Adjusted GF/GP Revenue Down 40% Since FY 2000



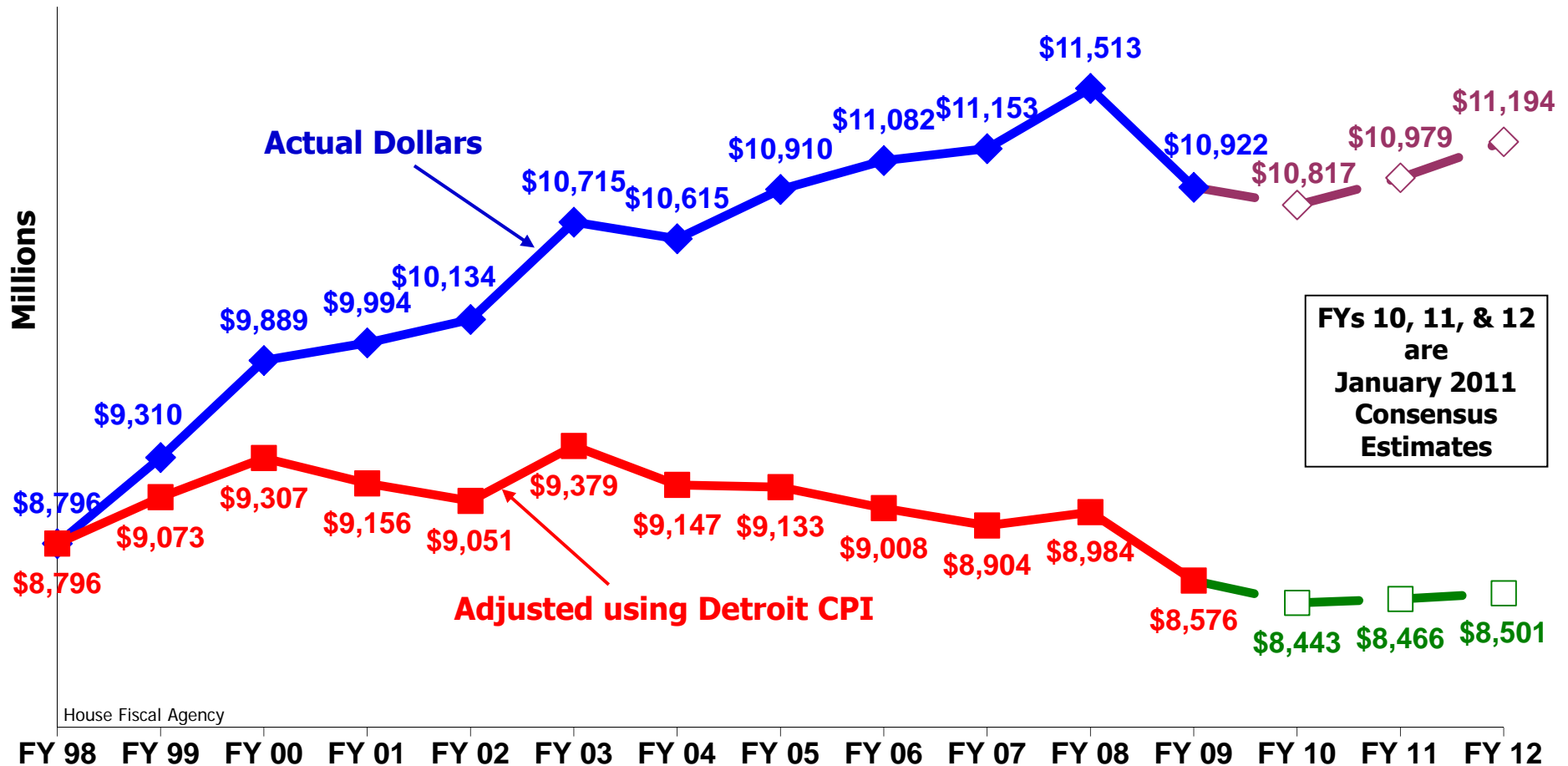


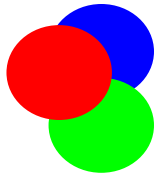
GF/GP Appropriations



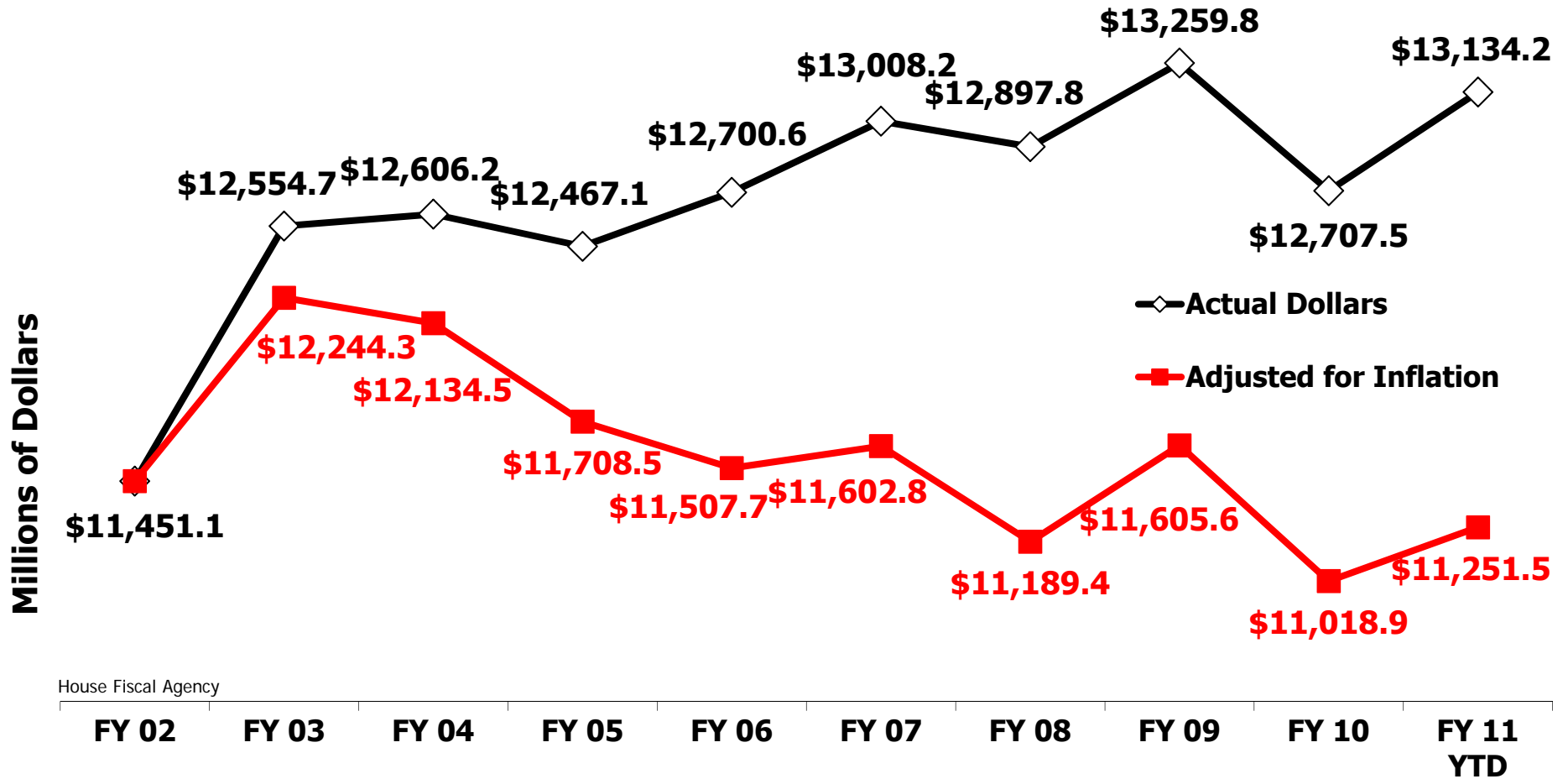


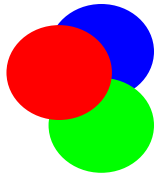
Inflation Adjusted SAF Net Revenue Down 8.7% Since FY 2000



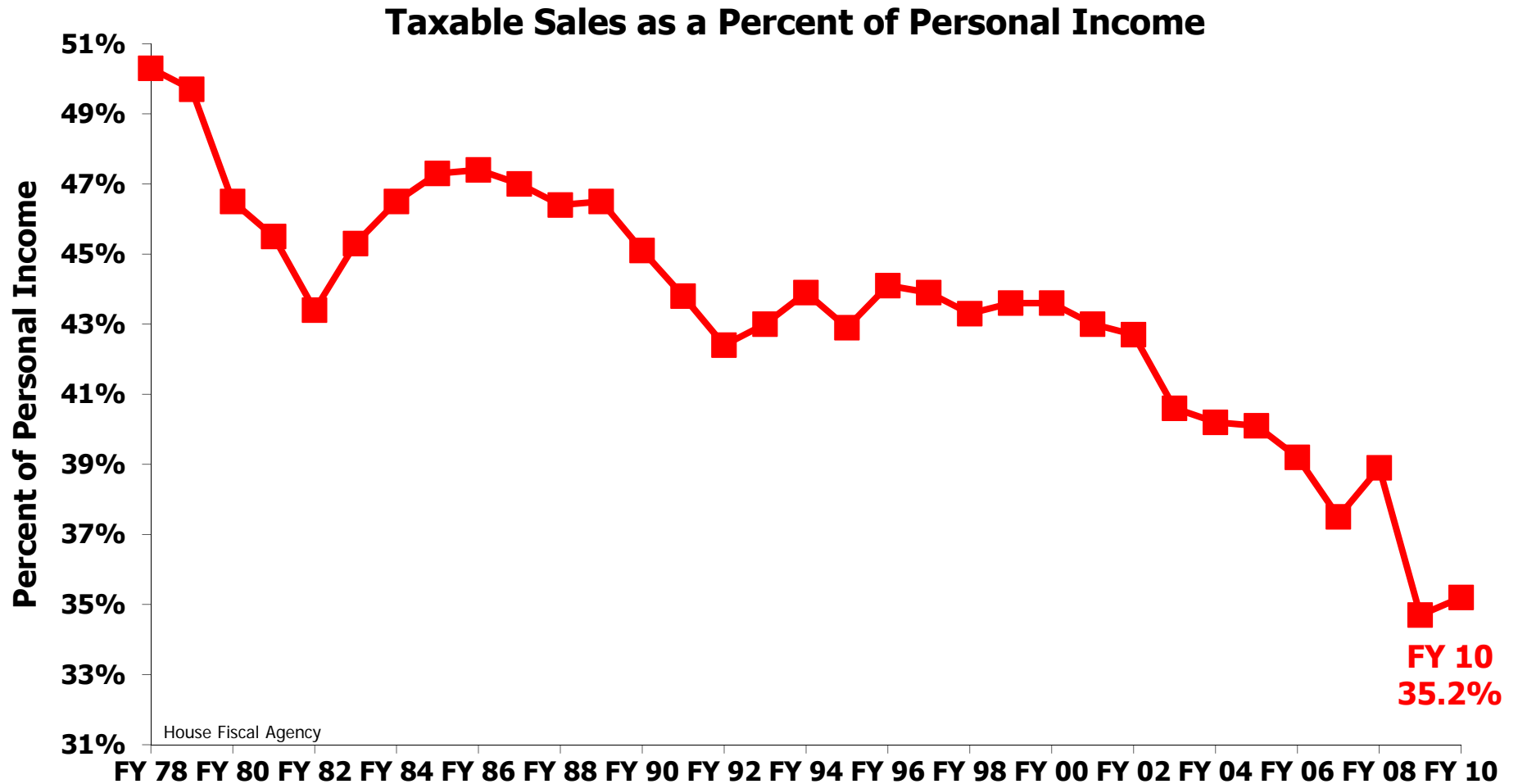


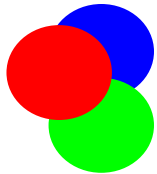
School Aid Budget Adjusted Gross Appropriations



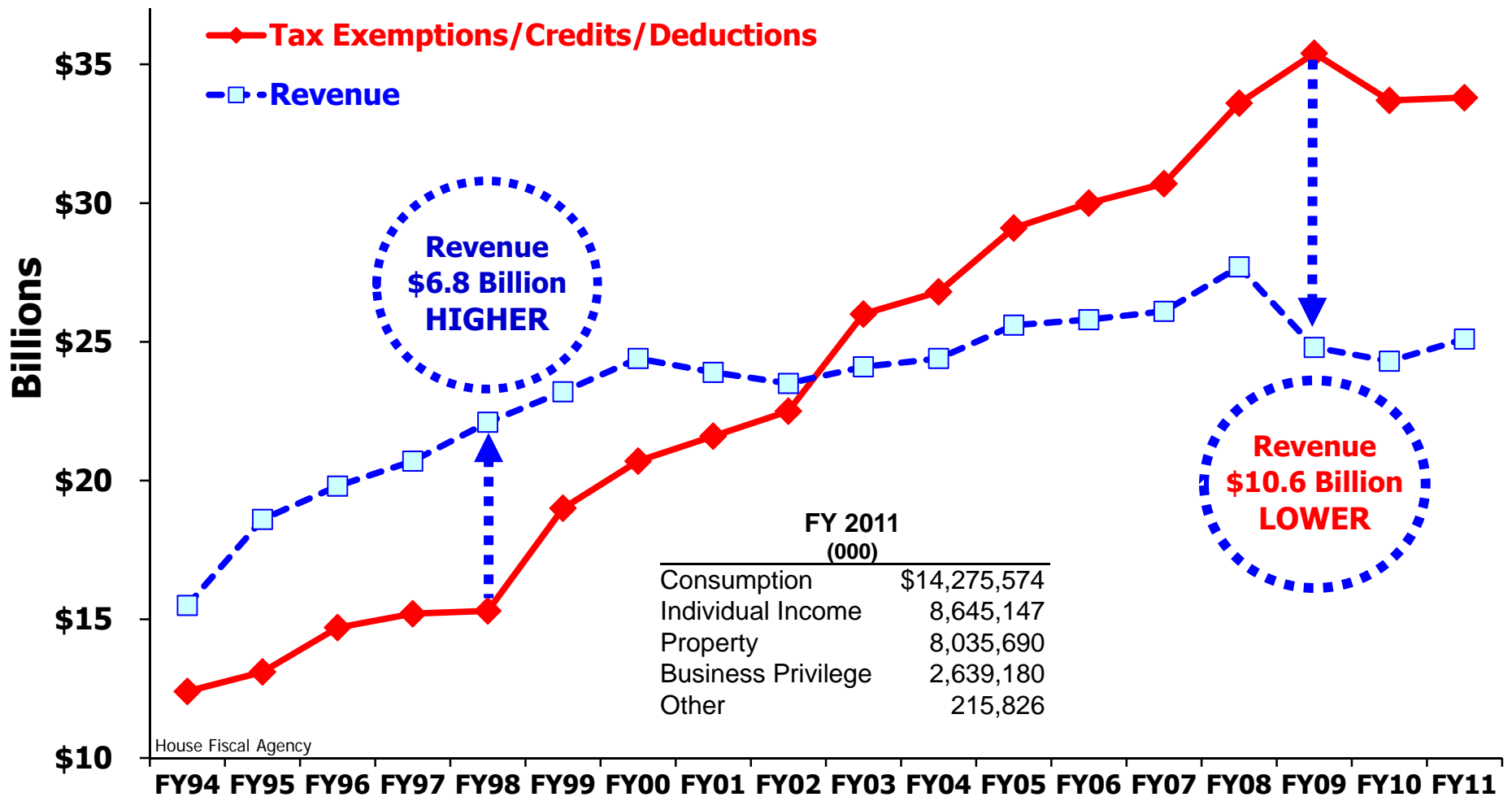


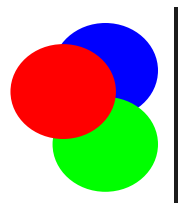
Sales/Use Tax Share Declining





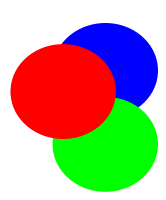
Impact of Tax Exemptions/Credits/Deductions





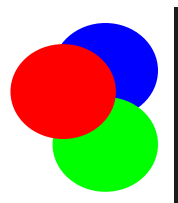
Why Consider Tax Expenditures?

- Tax expenditures are an alternative to direct spending.
- They can be used to effectively continue to spend tax dollars on policy initiatives while the budget is being reduced.
- They're "off-budget" for all practical purposes.
- Transparency and government accountability demand they be reported and evaluated.



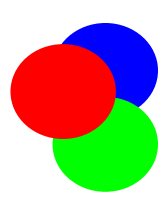
Impact of Recent Tax Cuts on Future Revenues

	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>
Reducing Michigan Income Tax Rate	\$0.0	\$0.0	\$0.0	(\$161.8)	(\$342.2)	(\$543.5)
Alternative Energy Credits - Income Tax	(\$16.0)	(\$22.6)	(\$24.2)	(\$18.9)	\$0.0	\$0.0
Michigan EITC	(\$140.0)	(\$341.0)	(\$357.0)	(\$378.0)	(\$400.7)	(\$424.8)
Eliminating MBT Surcharge	Eliminated in Tax Year 2017					
MBT Battery Credits (Assumes Maximum Used)	\$0.0	\$0.0	\$0.0	(\$40.0)	(\$268.0)	(\$278.0)
MBT Film Production Credit	(\$37.5)	(\$61.9)	(\$105.0)	(\$140.0)	(\$140.0)	(\$140.0)
Photovoltaic Technology - Facility & Manufacturing	\$0.0	\$0.0	(\$1.5)	(\$7.5)	(\$7.5)	(\$10.0)
Polycrystalline Manufacturing Credit	\$0.0	\$0.0	\$0.0	\$0.0	(\$20.0)	(\$25.0)
MBT Gross Receipt Changes	(\$115.8)	(\$80.5)	(\$93.4)	(\$117.8)	(\$129.9)	(\$132.7)
Decouple Bonus Depreciation/Production Activities	\$172.5	\$23.4	\$19.2	\$45.3	\$52.3	\$60.0
Historic Preservation Credits	\$0.0	\$0.0	(\$5.0)	(\$8.6)	(\$9.6)	(\$10.6)
Use Tax Bad Debt Deduction Change (Court Case)	(\$2.0)	(\$25.5)	(\$16.6)	(\$17.1)	(\$17.7)	(\$18.4)
Angel Credit	\$0.0	\$0.0	(\$3.4)	(\$9.0)	(\$9.0)	(\$9.0)
Exempt Supplies for Cobo Center	\$0.0	\$0.0	(\$2.5)	(\$2.5)	(\$3.5)	(\$1.5)
Totals in Millions	(\$138.8)	(\$508.1)	(\$589.4)	(\$855.9)	(\$1,295.8)	(\$1,533.5)



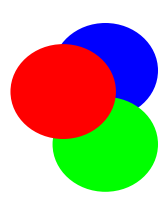
Fewer People Pay Income Tax

<u>All Filers</u>	<u>2000</u>	<u>2008</u>
Tax Liability < \$0	19.5%	25.6%
Tax Liability = \$0	8.0%	8.0%
<u>Tax Liability Between \$0 and \$100</u>	<u>6.1%</u>	<u>5.0%</u>
Tax Liability < \$100	33.6%	38.6%



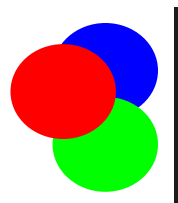
Refundable Credits on the Michigan Income Tax

- **Homestead Property Tax Credit (\$1,006.6 million in FY 2010-11)**
- **Earned Income Tax Credit (\$353.8 million in FY 2010-11)**
- **Alternative Energy/Qualified Home Improvement Credit (\$23.6 million in FY 2010-11) – sunsets in 2012**
- **Adoption Credit (\$0.8 million in FY 2010-11)**
- **Stillbirth Credit (\$39,000 in FY 2010-11)**



Indexed Provisions of the Michigan Income Tax

- **Personal Exemption**
- **Special Exemptions for Seniors and/or Disabled Individuals**
- **Special Exemption for Qualified Disabled Veterans**
- **Income Threshold for Pension Income Deduction**
- **Income Threshold for Deduction of Interest and Capital Gains Earned by Seniors**
- **Home Heating Credit**
- **Stillbirth Credit**



Impact of Shrinking Tax Base

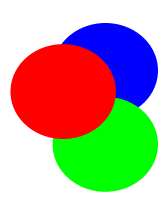
	<u>Income Tax Rate</u>	<u>Collections as Percent of State Personal Income</u>
FY 2000	4.0%	2.6%
FY 2010	4.35%	1.5%
Revenue Impact of Declining Base (In Millions of Dollars)		\$3,653.50

	<u>Sales and Use Tax Rate</u>	<u>Collections as Percent of State Personal Income</u>
FY 2000	6.0%	2.8%
FY 2010	6.0%	2.1%
Revenue Impact of Declining Base (In Millions of Dollars)		\$2,511.60



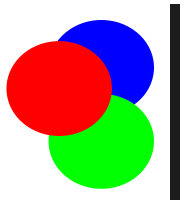
Structural Problems Began in Earnest in 2001

Funding Source	\$ Amount in Millions
■ Withdrawn from the BSF	\$1,264.0
■ SAF surplus	\$870.0
■ One-time revenue from changing SET collection dates	\$454.0
■ Other one-time revenue from various fund shifts and property sales	\$689.0
Total One-Time Revenue June 2001 to December 2002	\$3,277.0

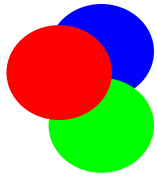


Structural Problems Continue in FY 2011

<u>Funding Source</u>	<u>\$ Amount in Millions</u>
■ Federal Funds	\$976.5
■ Tax Amnesty (\$88.8M in FY11 plus assumed \$20.5M loss in FY12)	\$109.3
■ Unclaimed Property (difference between FY11 and FY12)	\$107.0
■ Debt Service Restructuring (difference between FY11 and FY12)	\$162.2
■ Early Retirement (one-time replacement savings minus 3% phase-in)	\$24.0
■ County Revenue Sharing: Projected FY 2011-12 Increase	\$40.0
Total One-Time Funding Sources	\$1,419.0

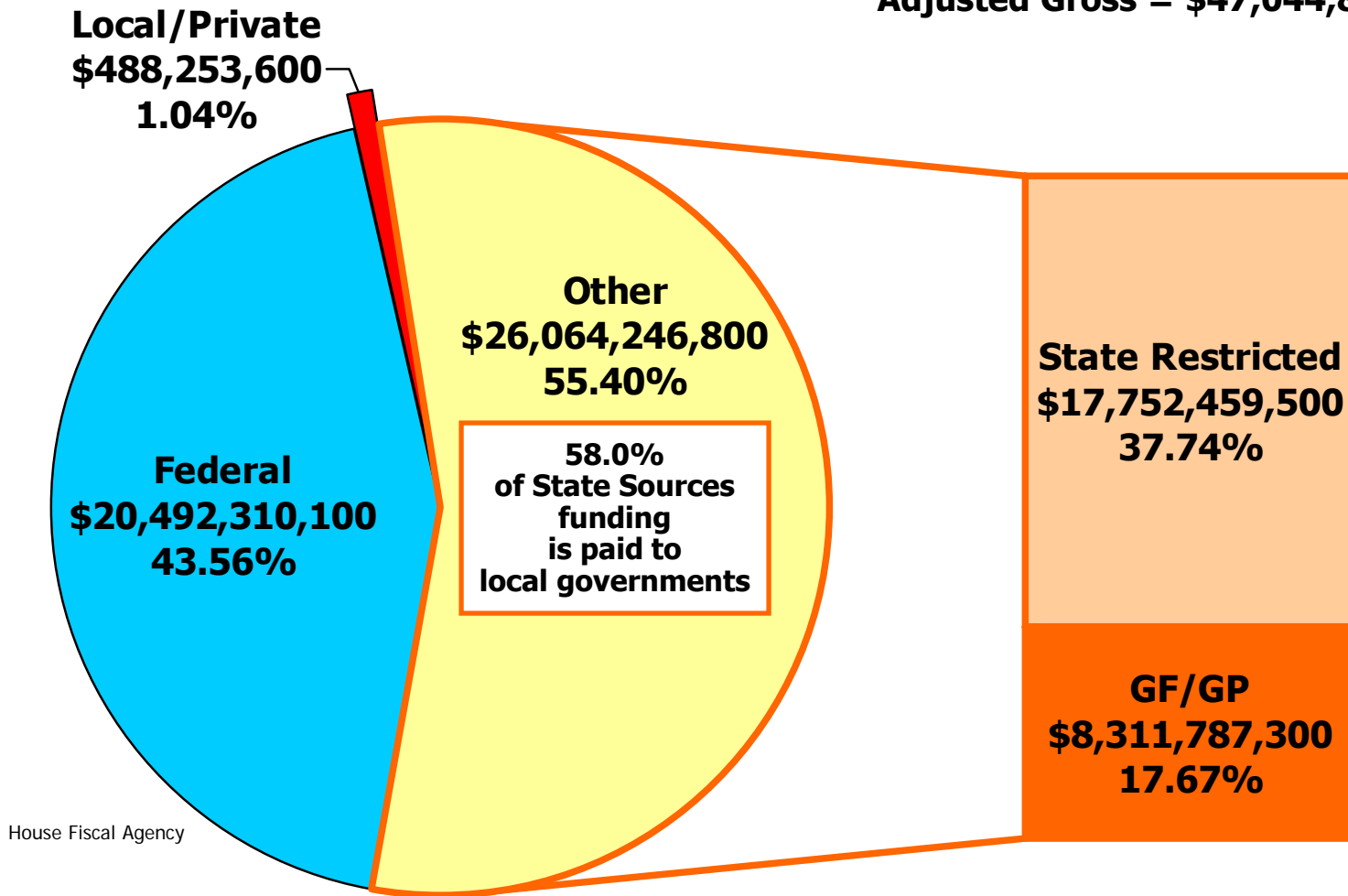


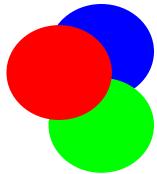
MICHIGAN'S CURRENT BUDGET



FY 2010-11 Budget Adjusted Gross Funding Sources

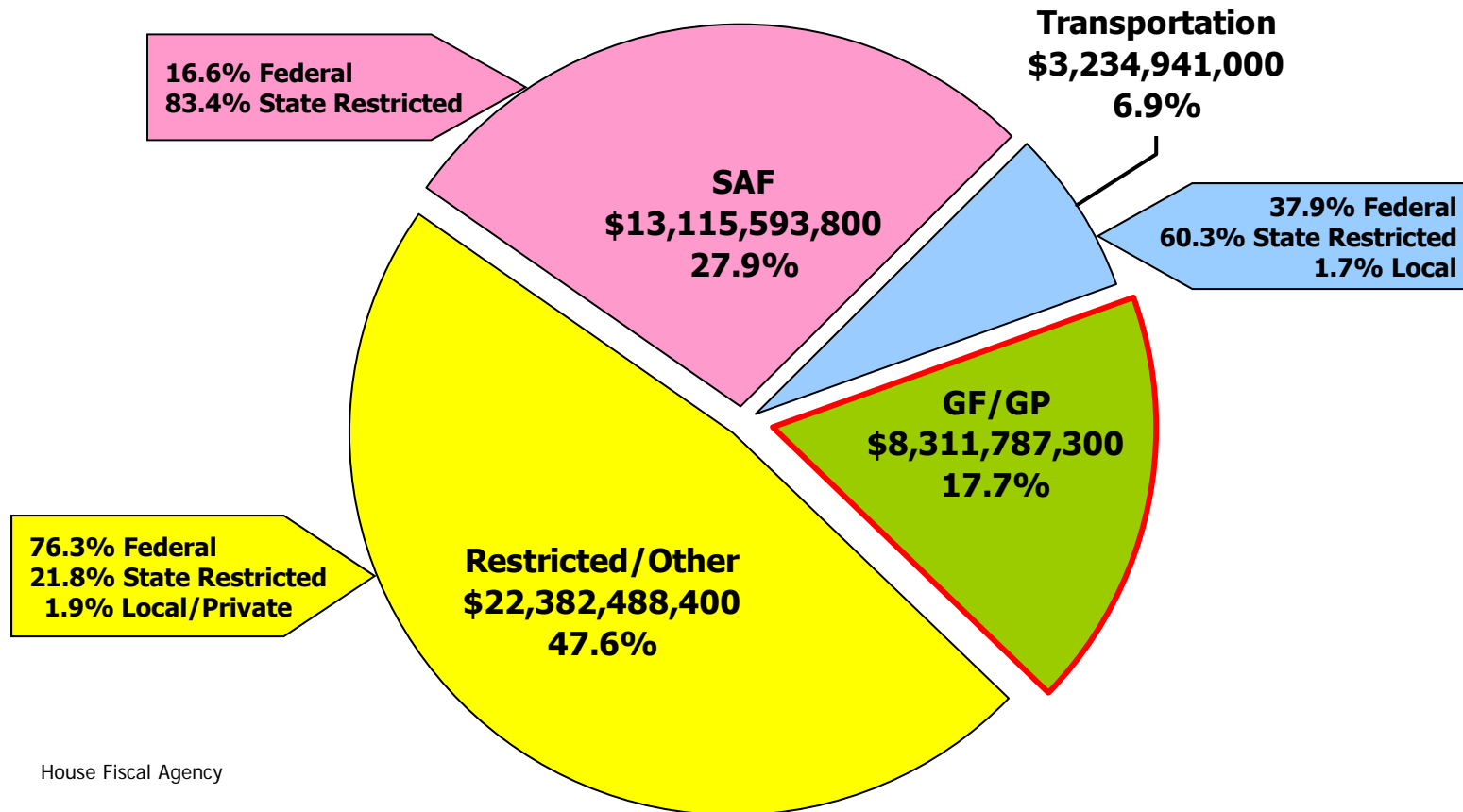
Adjusted Gross = \$47,044,810,500



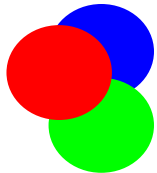


FY 2010-11 Appropriations Funding

Adjusted Gross = \$ 47,044,810,500

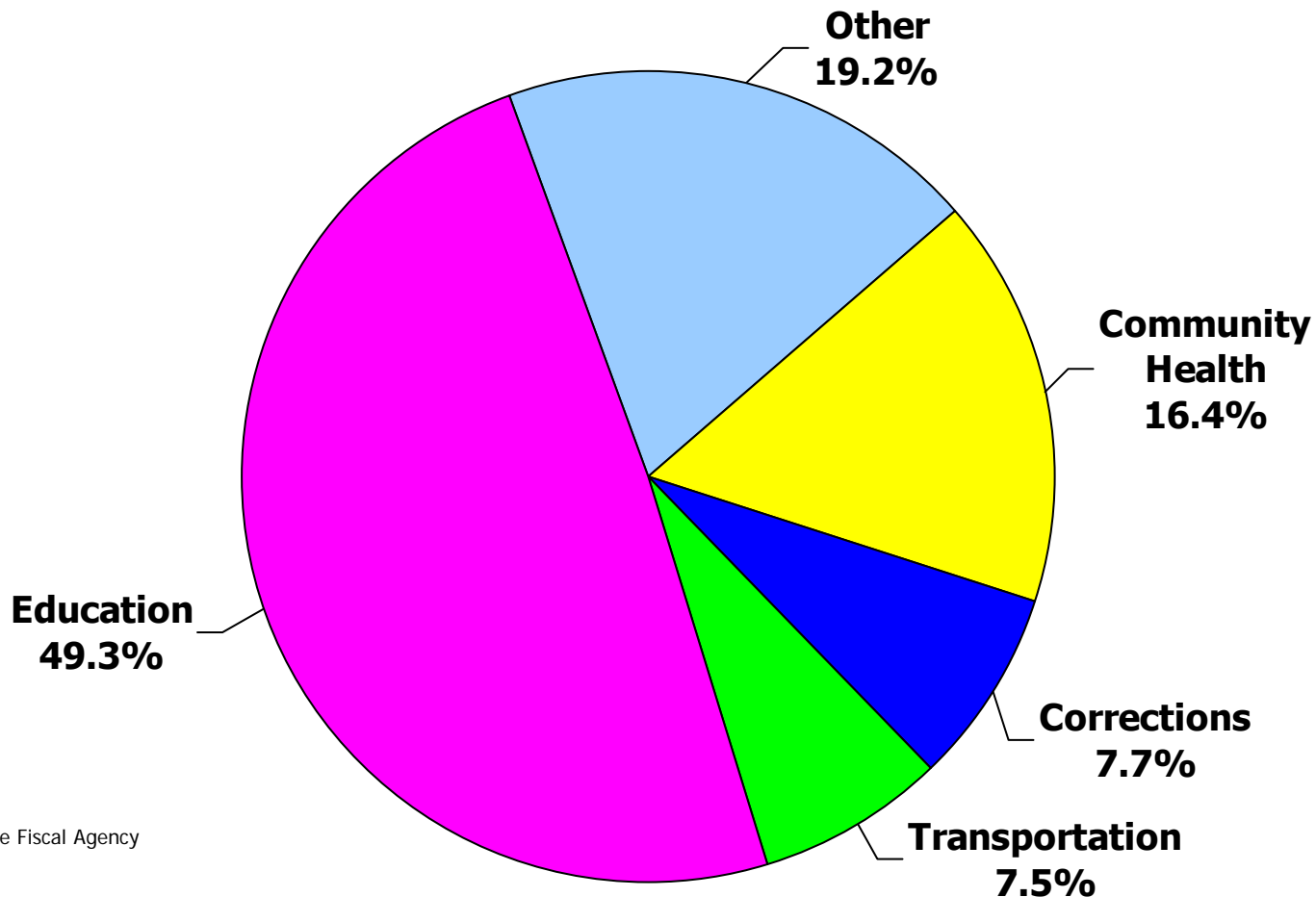


House Fiscal Agency

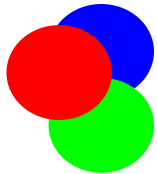


State Tax and Fee Revenue FY 2010-11

FY 2010-11 Total = \$26,064,246,800

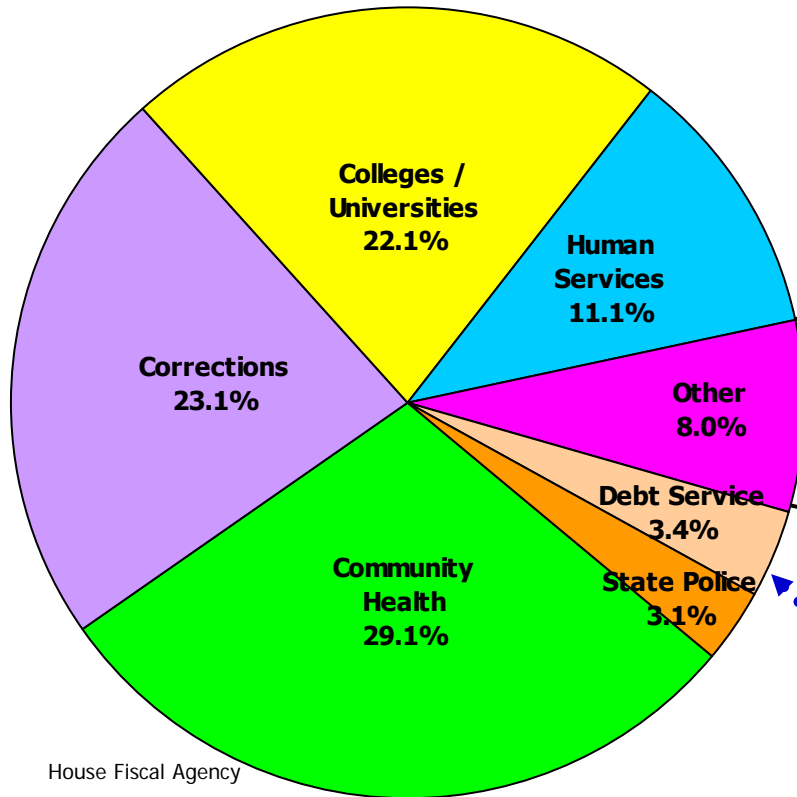


House Fiscal Agency

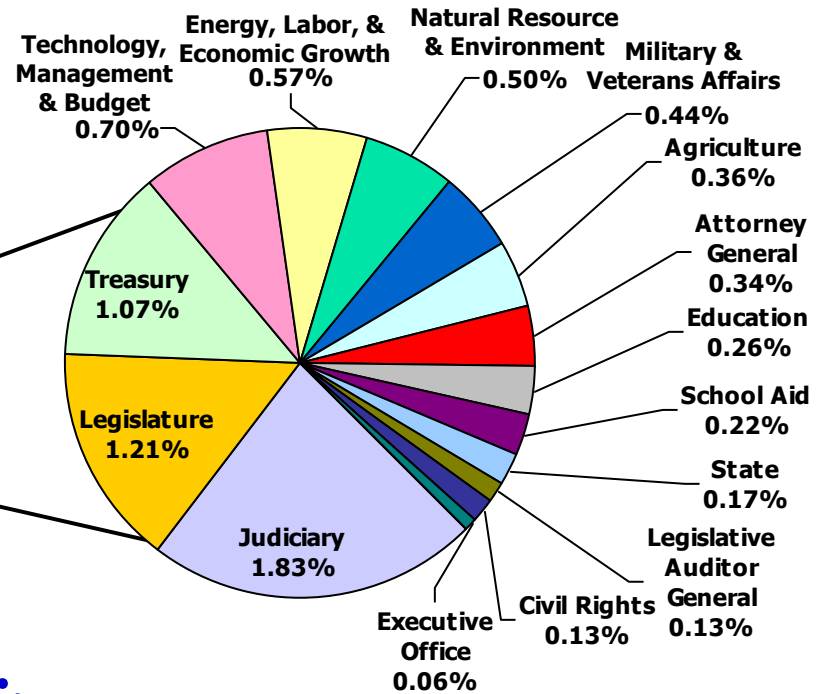


FY 2010-11 GF/GP

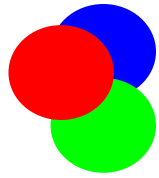
FY 2010-11 Total = \$8,311,787,300



House Fiscal Agency



3.4%
\$284 million
Debt Service and SBA Rent

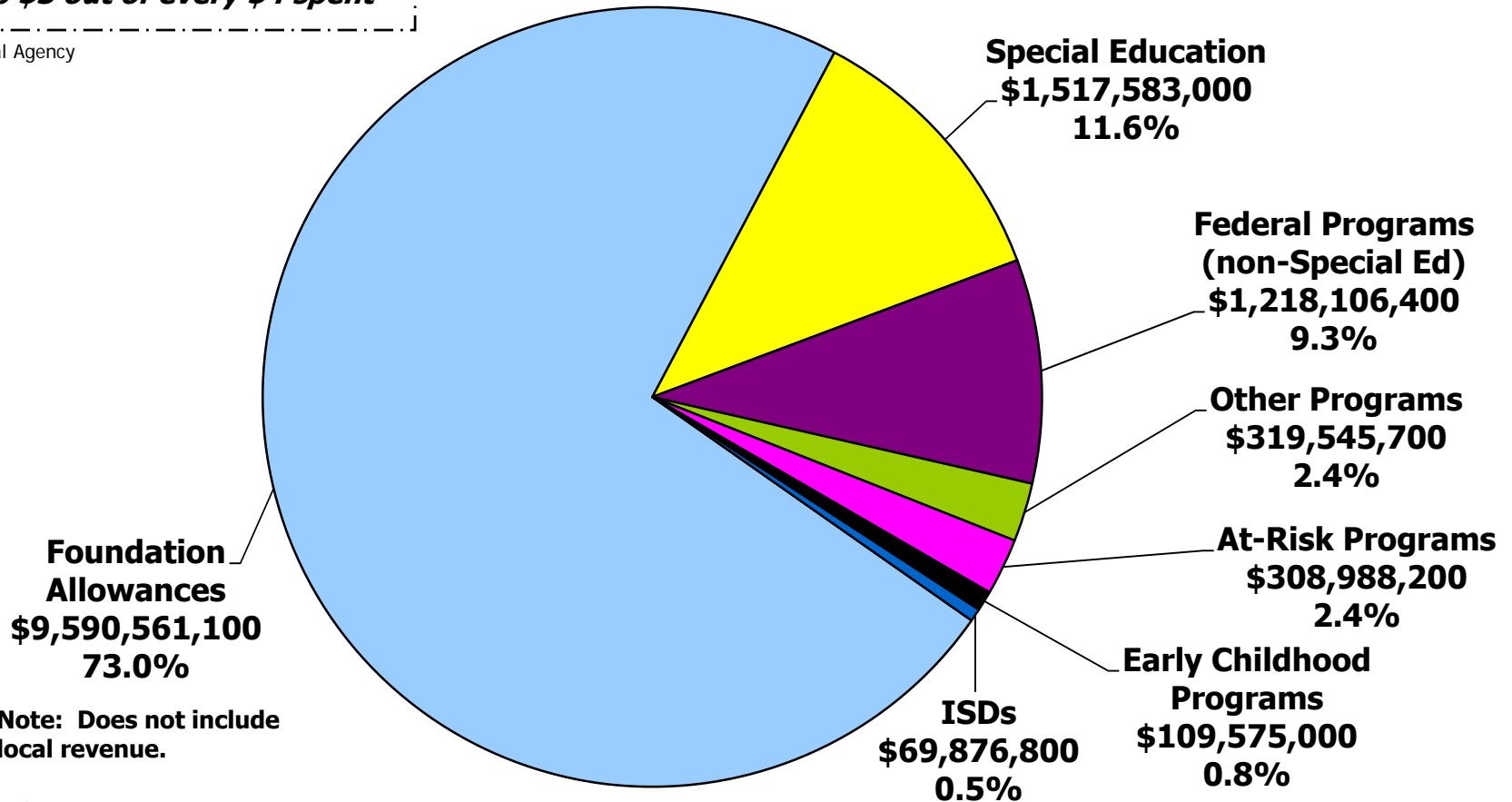


School Aid Major Spending Categories

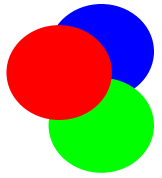
FY 2010-11 Total = \$13,134,236,200

*Foundation allowances
(used for school operations)
absorb \$3 out of every \$4 spent*

House Fiscal Agency

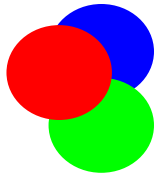


Note: Does not include local revenue.

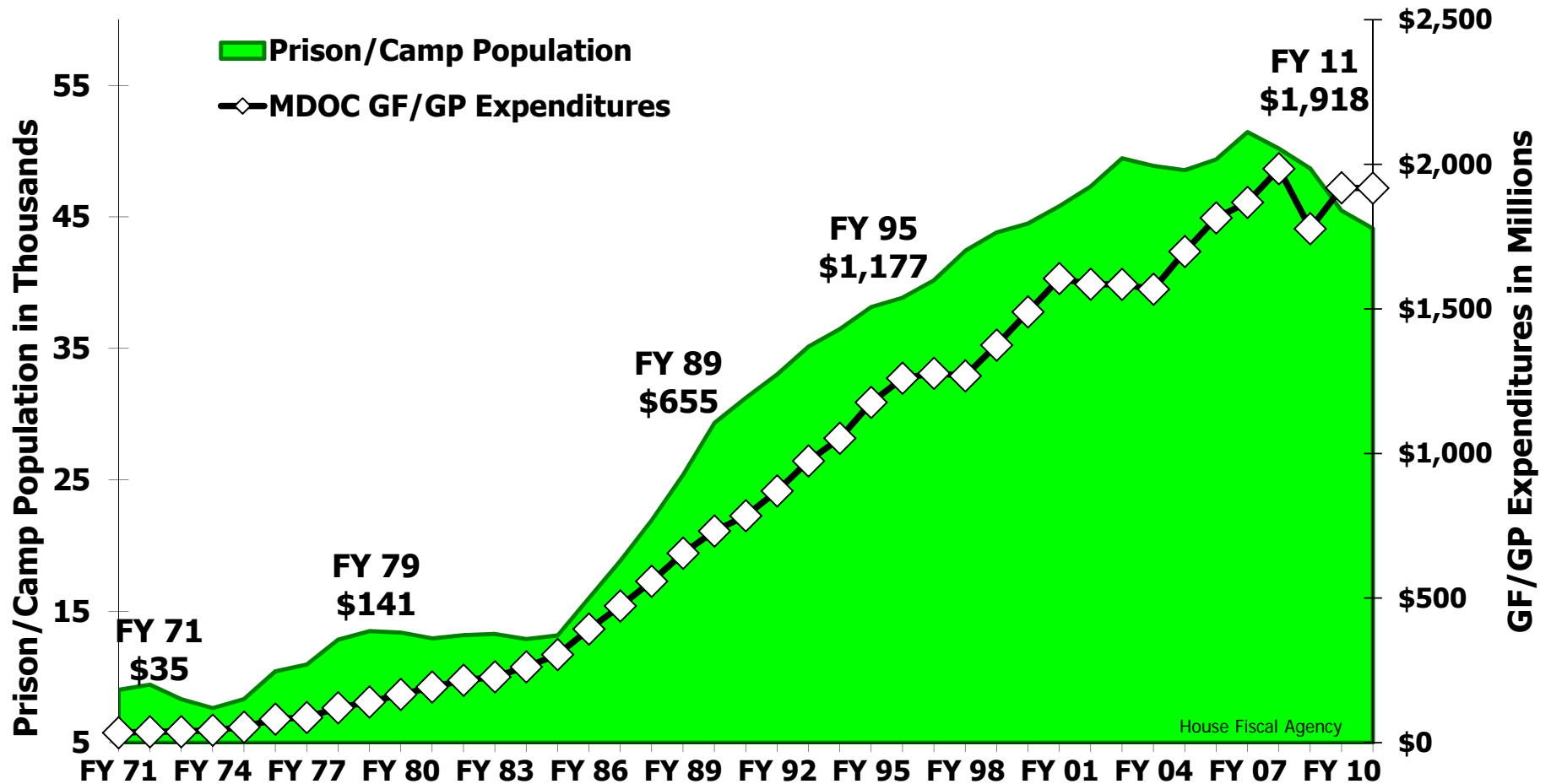


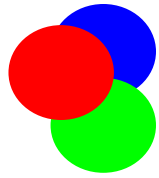
Medicaid Impact on Michigan Budget

- For FY 11, approximately 19.1% of Michigan GF/GP revenue is appropriated for Medicaid
- 1 of 6 Michigan residents were eligible for Medicaid in April 2009
- 42% of births and 70% of nursing home expenditures in Michigan are financed through Medicaid
- Total state and federal Medicaid appropriation is over \$11.5 billion in FY 11
- Since FY 1999-2000
 - 126.5% increase in Medicaid funding
 - 71.5% growth in Medicaid caseload (759,800 cases)

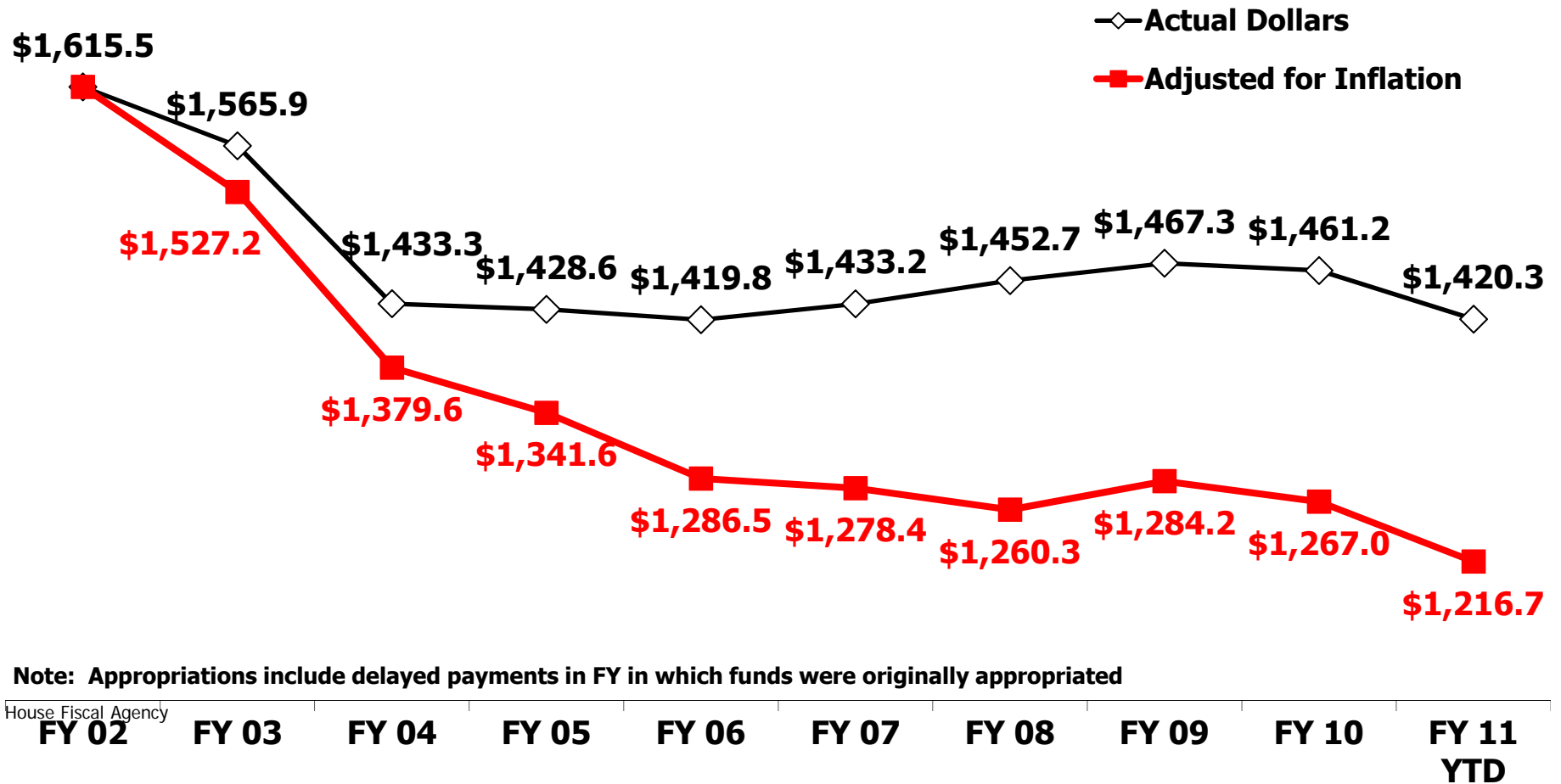


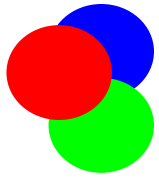
Corrections Budget Increases



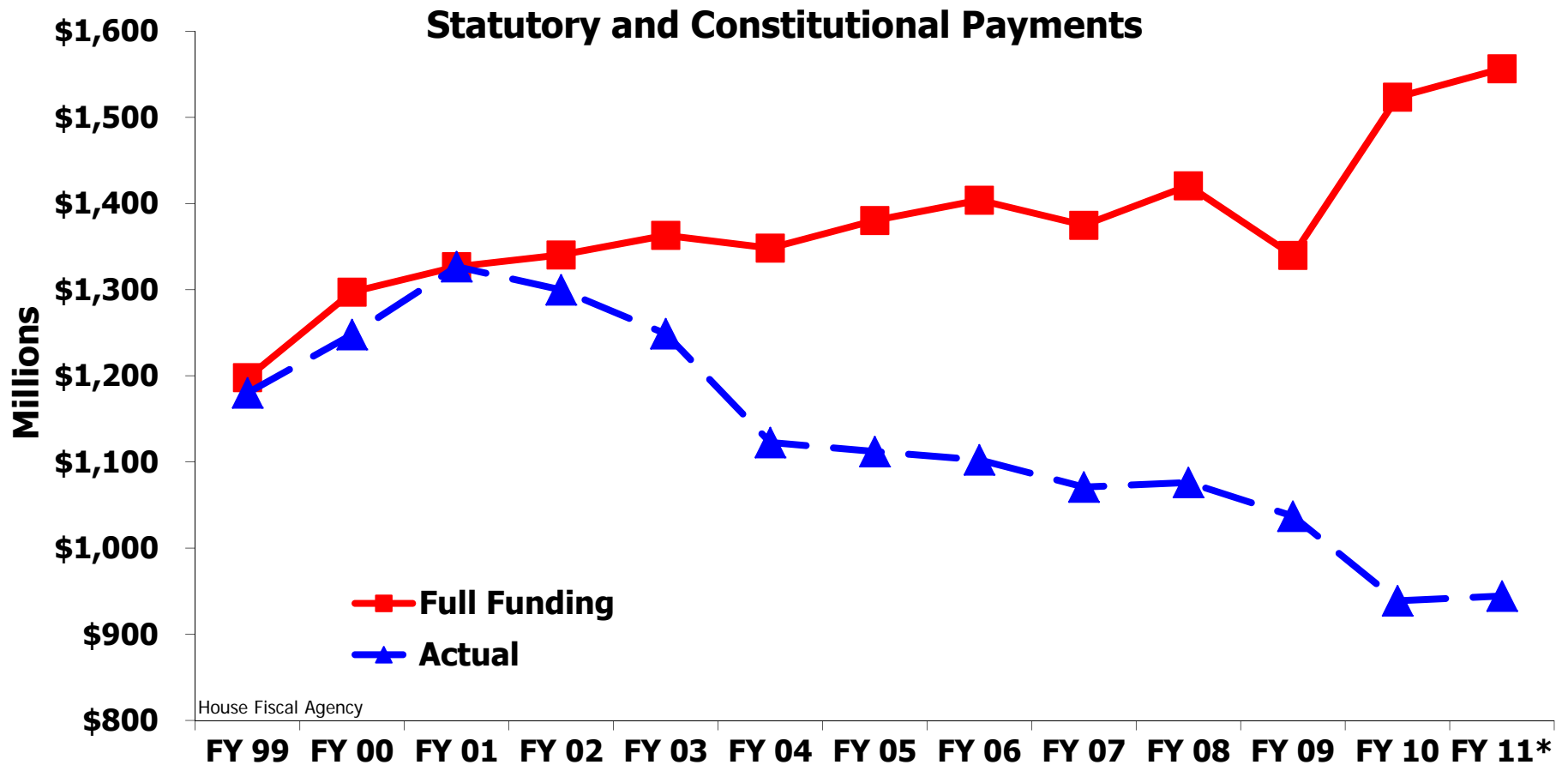


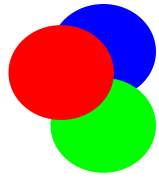
Total Appropriations for State University Operations





Revenue Sharing Payments to Cities, Villages, and Townships

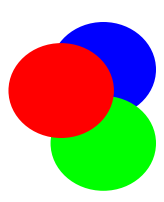




Property Value Growth Slowing

Yearly Change

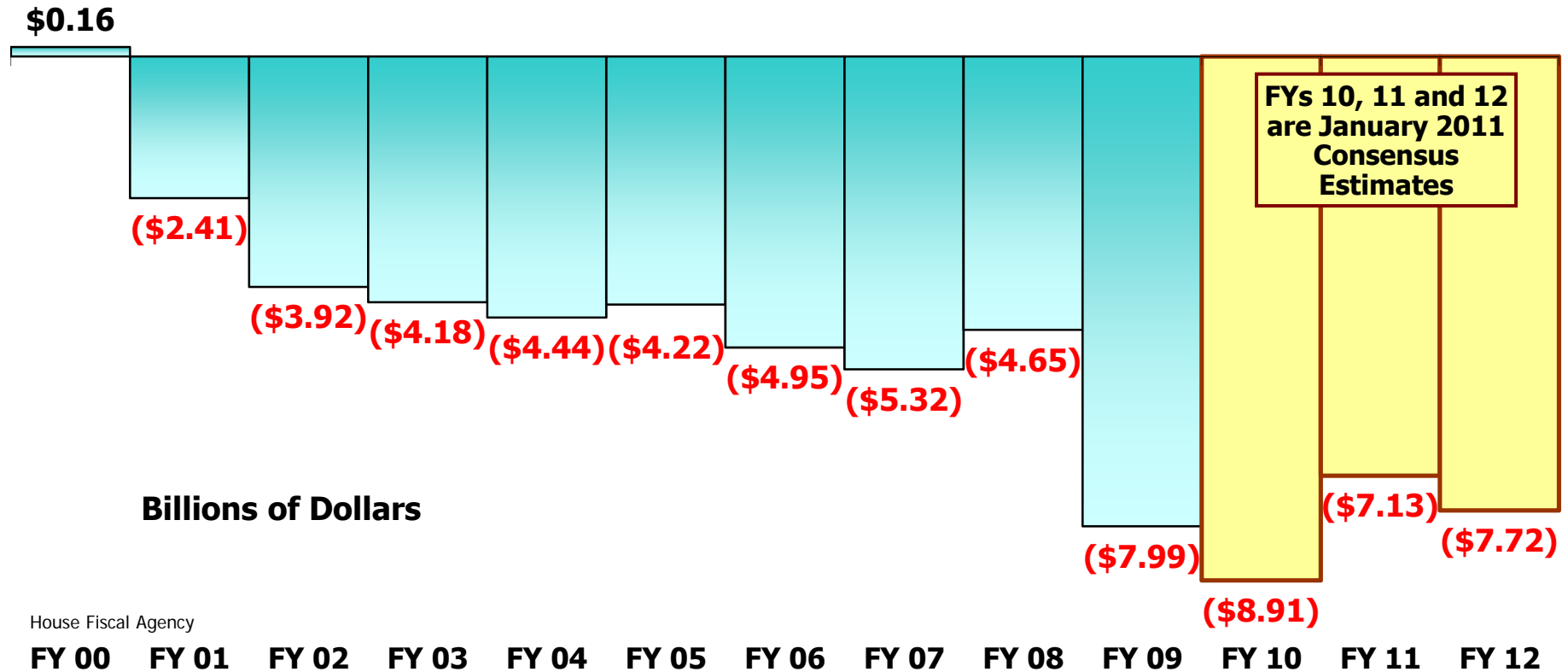
	<u>Inflation Rate Multiplier for Property</u>	<u>Total SEV Growth</u>	<u>Total Taxable Value Growth</u>
1997	2.8 %	8.2 %	5.7 %
1998	2.7 %	9.5 %	6.1 %
1999	1.6 %	9.9 %	6.0 %
2000	1.9 %	9.0 %	5.5 %
2001	3.2 %	10.0 %	7.1 %
2002	3.2 %	9.8 %	6.7 %
2003	1.5 %	7.5 %	4.8 %
2004	2.3 %	6.3 %	5.7 %
2005	2.3 %	5.9 %	5.6 %
2006	3.3 %	5.0 %	5.8 %
2007	3.7 %	3.8 %	5.2 %
2008	2.3 %	-1.1 %	1.4 %
2009	4.4 %	-5.4 %	-0.8 %
2010	-0.3 %	-9.2 %	-6.6 %
2011	2.5 %	N/A	-4.3 %



Constitutional Revenue Limit

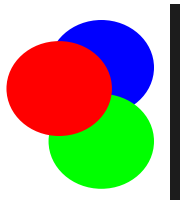
Average growth of Michigan personal income = 2.0% per year from 2000 through 2012

Average increase of Michigan revenue = 0.4% per year from 2000 through 2012

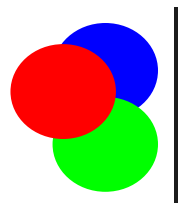


House Fiscal Agency

FY 00 FY 01 FY 02 FY 03 FY 04 FY 05 FY 06 FY 07 FY 08 FY 09 FY 10 FY 11 FY 12



EXECUTIVE BUDGET RECOMMENDATION



Total Budget Cuts \$1,520.9 Million

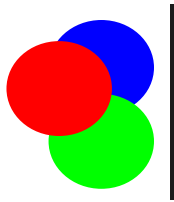
- Corrections (\$51.2 million)
- Community Health (\$212.6 million)
- Human Services (\$109.5 million)
- Higher Education (\$222.4 million)
- Statutory Revenue Sharing (\$143.9 million)
- State employee concessions (\$180.0 million)
- Other (\$63.2 million)
- School Aid reductions (\$538.1 million)



School Aid Cuts

- **Reduces Foundation Allowances by \$470 Per Pupil**
 - **Makes the FY 2011 \$170 per pupil reductions permanent by rolling the cut into the foundation allowance**
 - **Reduce all foundations by \$300 per pupil, for a total foundation allowance reduction of \$470 per pupil**
 - **Additional \$300 per pupil cut equals a savings of \$452.5 million**

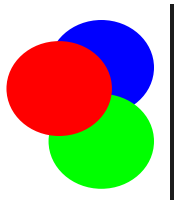
- **Certain Categorical Funding programs eliminated – totaling \$82.8 million**



School Aid Cuts

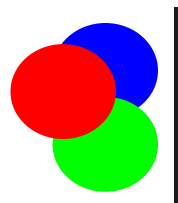
- **Intermediate School District (ISD) General Operations**
 - **Reduces payments by 5% or \$3.3 million**

- **School Aid Fund (SAF) Revenue Shifts Totaling \$1.1 Billion**
 - **Tax proposal reduces SAF revenue (\$597.1)**
 - **Budget proposal increases GF/GP transfer to SAF (\$393.9)**
 - **SAF revenue shifted into Community College budget (\$195.9) and Higher Education budget (\$699.7 million)**



Higher Education

- **Each university's appropriation is reduced by 15% (\$222.4 million GF/GP)**
- **Tuition restraint incentive funding (\$83 million)**
 - **Funds would be paid only if a university held its FY 2011-12 resident undergraduate tuition/fee increases below the prior-five-year state average**
 - **Individual incentive amounts (based on average annual tuition/fee rate increase over the last five years) ranging from 5.1% to 9.8% of proposed FY 2012 appropriation amounts**



Revenue Sharing Cuts

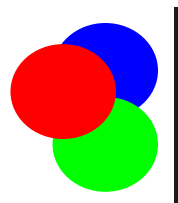
- **Statutory Revenue Sharing line item for cities, villages, and townships (CVT's) eliminated and replaced by Local Government Incentives Program**
 - **Revenue distributed to units that use "Best Practices"**
 - **Net reduction in funding (\$107.1 million)**

- **County Revenue Sharing**
 - **Distributed on a pro-rata basis for those who qualify, and is reduced \$14.7 million from FY 2011**
 - **Total reduction from current law is \$51.7 million**



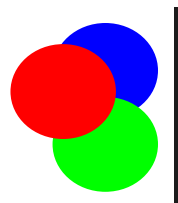
Local Government Incentives Program

- **Total of \$200 million: \$195 million to CVTs that meet criteria, \$5 million to defray consolidation costs**
- **No amount less than \$6,000 distributed. CVTs that receive less are not eligible**
- **Eligibility to receive distributed based on transparency, consolidation of services, employee compensation**



Other Cuts

- **Retroactive 48 month lifetime limit for cash assistance recipients (FIP)**
 - **Will close 12,600 FIP cases generating \$77.4 million gross, \$65.0 million GF/GP, in savings**
 - **Graduate Medical Education (GME) reduced 40%, \$67.3 million Gross (\$22.8 million GF/GP)**
- **Reduce Fire Protection Grant reduces grant payments to local units with state property (\$1.6 million)**
- **Reduces state aid to libraries by \$2.3 million (DOE)**
 - **Additionally, the School Aid budget eliminates \$1.5 million in state aid to libraries**



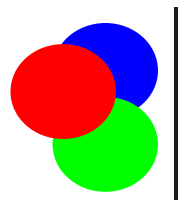
Latest Proposed Tax Plan

■ Net Revenue Reductions

- Reduce total revenue \$453.8 million in FY 2011-12 [GF/GP up \$225.7 million, SAF down \$679.5 million]
- Reduce total revenue \$192.0 million in FY 2012-13 [GF/GP up \$465.0 million, SAF down \$657.0 million]

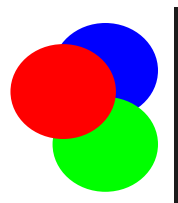
■ Cut business taxes \$1.67 billion

■ Increase personal income tax \$1.48 billion



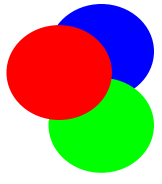
Business Tax Changes

- **Cut business taxes \$1.67 billion [82% net cut]**
- **Repeal the Michigan Business Tax**
- **Institute a 6% tax on business income for C corps only**
- **Honor existing firm-specific credits including MEGA, film, next energy, battery credits, etc.**



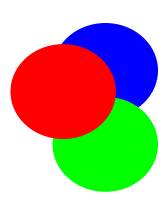
Personal Income Tax Changes

- **Increase personal income tax \$1.48 billion [26% net increase 2012]**
- **Suspend rate reduction from 4.35% to 4.25% until January 1, 2013 (a 15-month delay) [increases FY 13 revenue \$213.5 million]**
- **Reduce private non-military pension exemption [increases revenue \$342.8 million]**
- **Eliminate state earned income tax credit, EITC, [increases revenue \$373.7 million]**
- **Reduce homestead property tax credits [increases revenue \$202.5 million]**



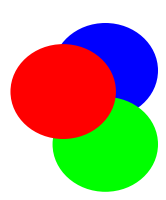
Personal Income Tax Changes

- **Eliminate special exemptions for seniors and UI and child deductions.**
- **Eliminate all other major refundable and non-refundable credits except for the homestead property tax credit and the home heating credit.**
- **The personal exemption will be set to \$3,700 and indexed to inflation beginning in 2013. The exemption would be phased out if "total household resources" exceed \$75,000 for a single filer or \$150,500 for joint filers.**



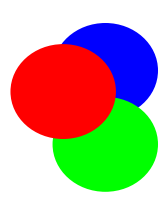
Non-Military Pension / Retirement Income (Proposed)

- **Taxpayers > 67 will be unaffected other than the loss of the senior exemption**
- **Taxpayers between 60 and 66 will receive the \$20,000/\$40,000 pension exemption (social security not taxed)**
- **They also continue to receive the new \$3,700 personal exemption – phased out if “total household resources” exceed \$75,000 single/\$150,000 joint**



Non-Military Pension / Retirement Income (Proposed)

- **Taxpayers < 60 no pension exemption until age 67**
- **Social security not taxable at the federal level is exempt**
- **At age 67, they will receive the \$20,000/\$40,000 exemption against all forms of income (social security / pension / retirement / wages)**
- **If social security alone exceeds \$20,000/\$40,000 – all is exempt**



Homestead Property Tax Credit (HPTC) Changes (Proposed)

- **HPTC increased for taxpayers with household incomes below \$30,000 and eliminated for taxpayers over \$50,000, or if taxable value is greater than \$200,000**
 - **For household income less than \$20,000, the credit equals the amount by which 100% of property taxes paid exceeds 3.5% of household, up to \$1,200**
 - **For household income between \$20,000 and \$30,000, the property tax factor phases down from 100% to 60% (the current limit)**
 - **The credit phases out between \$41,000 and \$50,000**



Summary of Executive Recommendation

- **Cut services \$1.5 billion to address the budget shortfall**
- **Provide a \$1.7 billion [82%] net tax cut for business**
- **Replace business tax revenue with \$1.5 billion [26%] increased income tax revenue by eliminating income tax expenditures**

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