

# Michigan's Economy and Budget

Prepared for:  
Grand Valley Metro Council

October 28, 2010



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## One-Time Funding Sources Utilized in FY 2011-12 Budget

<u>Funding Source</u>	<u>\$ Amount by Affected Fund (Millions)</u>
	<u>GF/GP</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)	\$15.0
■ County Revenue Sharing: Projected FY 2011-12 Increase	\$40.0
<b>Total One-Time Funding Sources</b>	<b>\$1,410.0</b>
Impact of Enacted Tax Cuts on FY 2011-12 Revenue	\$210.4
<b>Total Structural Issues for FY 2011-12 Budget</b>	<b>\$1,620.4</b>





## One-Time Funding Sources Utilized in FY 2011-12 Budget

Funding Source	\$ Amount by Affected Fund (Millions)	
	School Aid	Transportation
■ ARRA Funds in School Budget	\$184.3	
■ Ed Jobs Funds for School Aid*	\$318.1	
■ Transportation: Debt Restructuring		\$84.0
<b>Total One-Time Funding Sources</b>	<b>\$502.4</b>	<b>\$84.0</b>
Impact of Enacted Tax Cuts on FY 2011-12 Revenue	\$6.0	\$0.0
<b>Total Structural Issues for FY 2011-12 Budget</b>	<b>\$508.4</b>	<b>\$84.0</b>

\* Note: Not built into foundation



## UI Trust Fund

- Interest payments on \$3.8 billion of UI Trust Fund borrowing
  - Approximately \$150 million due September 30, 2011
    - State share approximately \$100 million
  - It will take a decade or more to pay down this debt

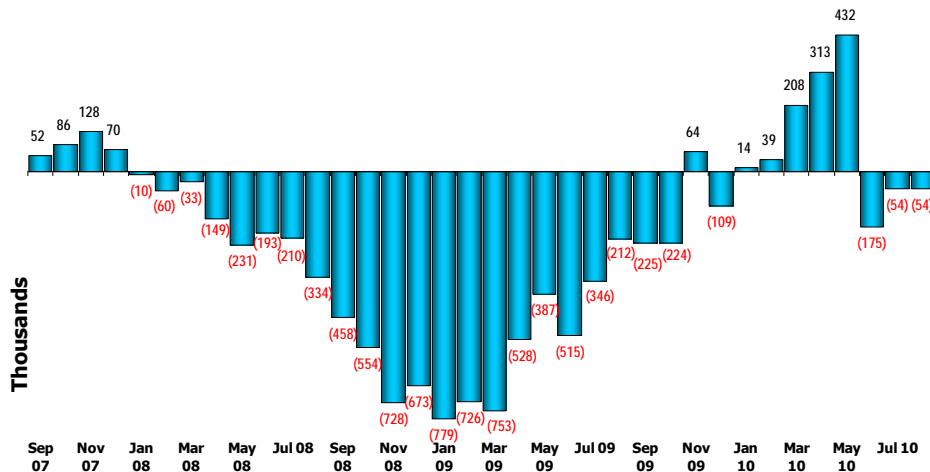


# State Budget Shortfalls Caused By

- Severe economic contraction led by domestic auto industry
- State tax policy
- Increasing cost of Medicaid and corrections

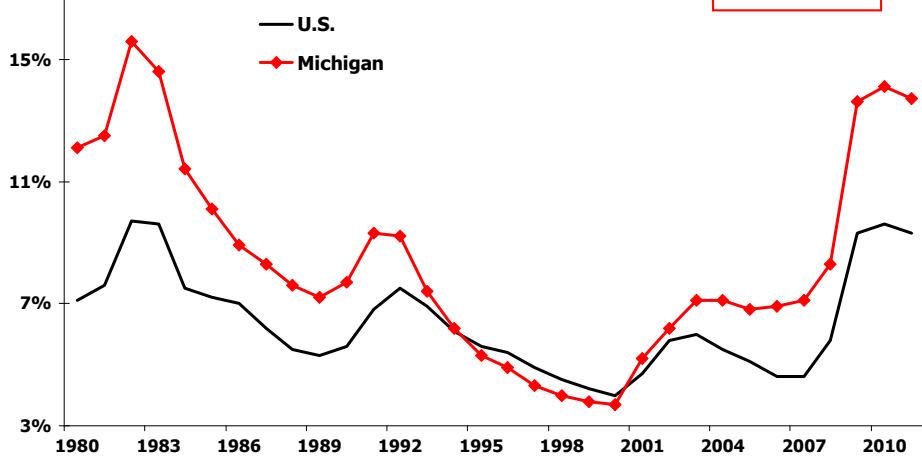


# U.S. Economy Lost 7.6 Million Jobs Since Recession Began





# U.S. and Michigan Unemployment Rates

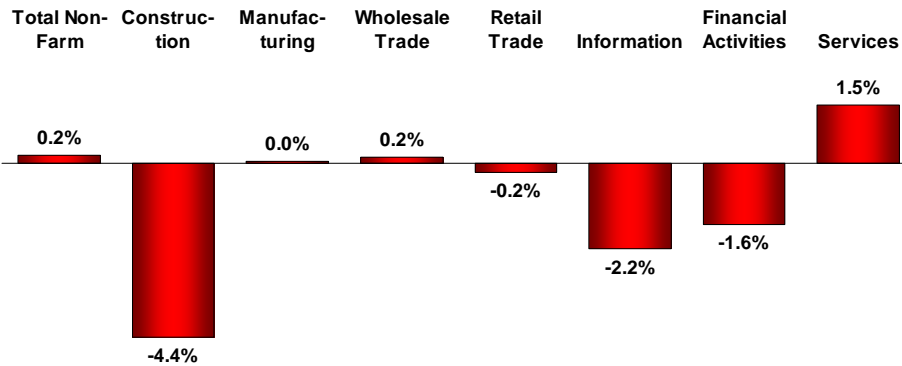


Sources: U.S. Bureau of Labor Statistics and May 2010 Consensus Estimates

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# U.S. % Change in Employment August 2009 Through August 2010



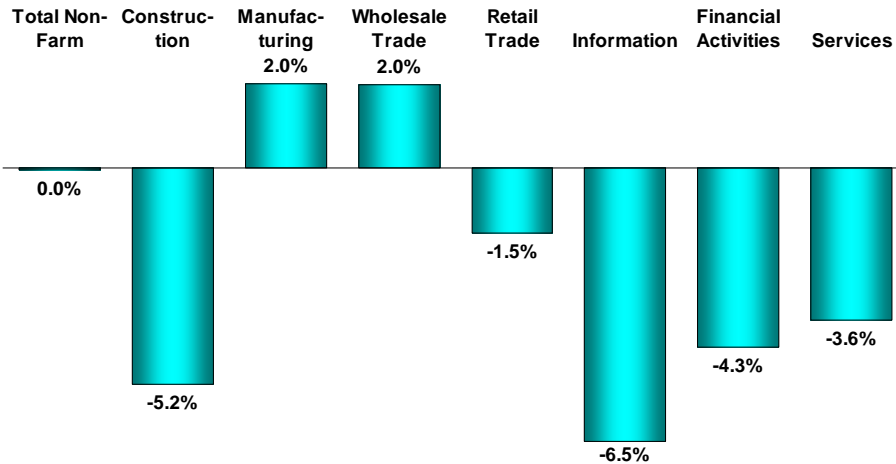
Source: U.S. Bureau of Labor Statistics

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## Michigan % Change in Employment

August 2009 Through August 2010



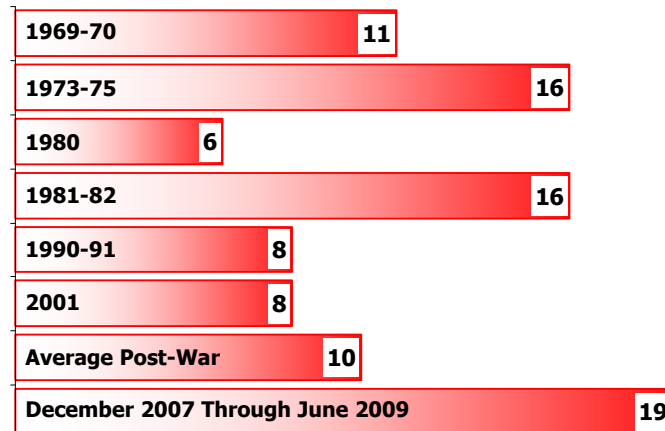
Source: U.S. Bureau of Labor Statistics

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## Length of U.S. Recessions

# of Months From Peak to Trough



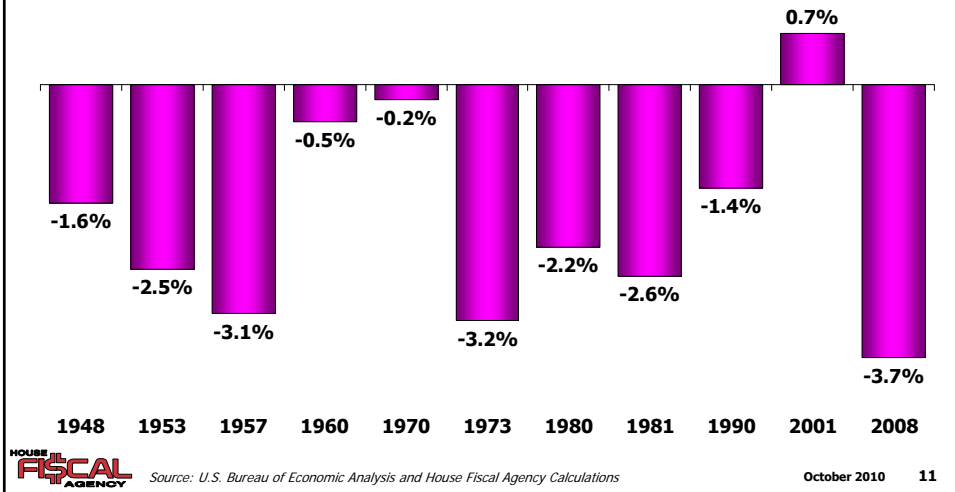
Source: National Bureau of Economic Research and IHS Global Insight, January 2010 Forecast

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## Decline in GDP Steep Compared to Recent Recessions

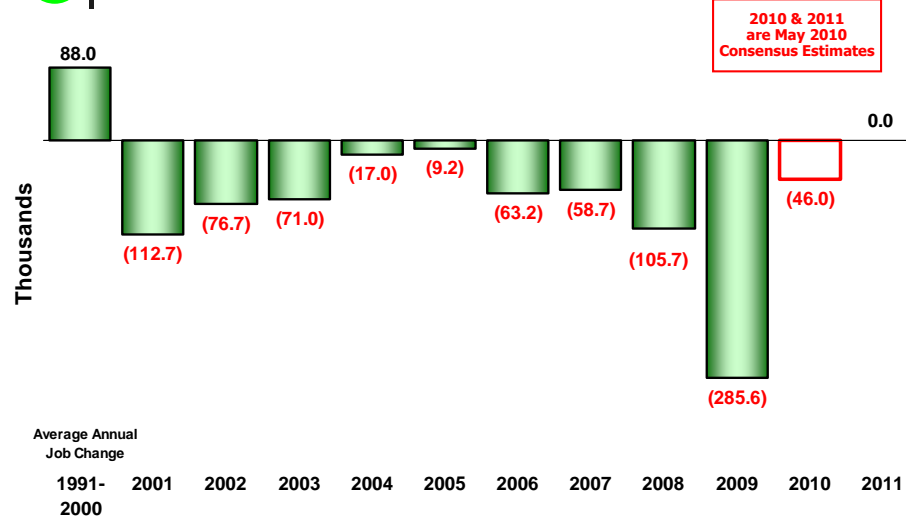
Peak to Trough GDP Decline



## MICHIGAN FORECAST



# Job Change in Michigan

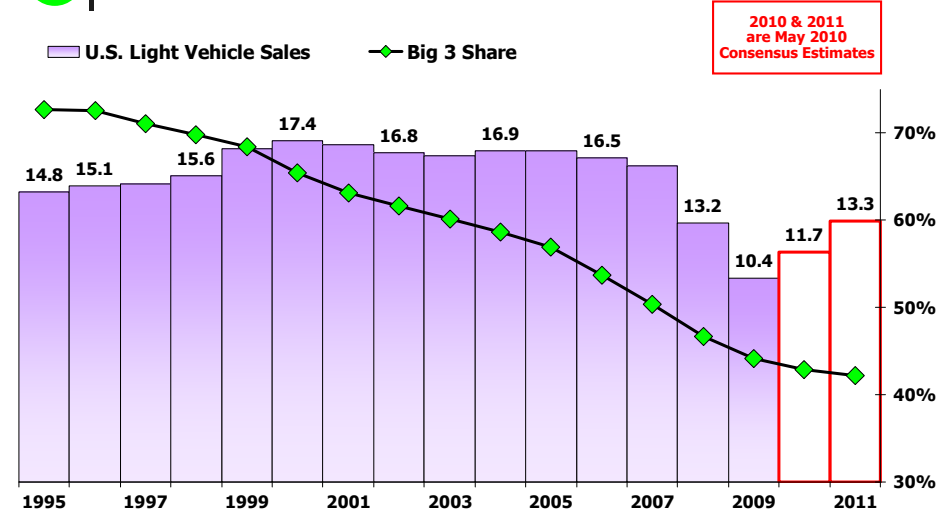


Source: U.S. Bureau of Labor Statistics and May 2010 Consensus Estimates

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# Big 3 Losing Market Share

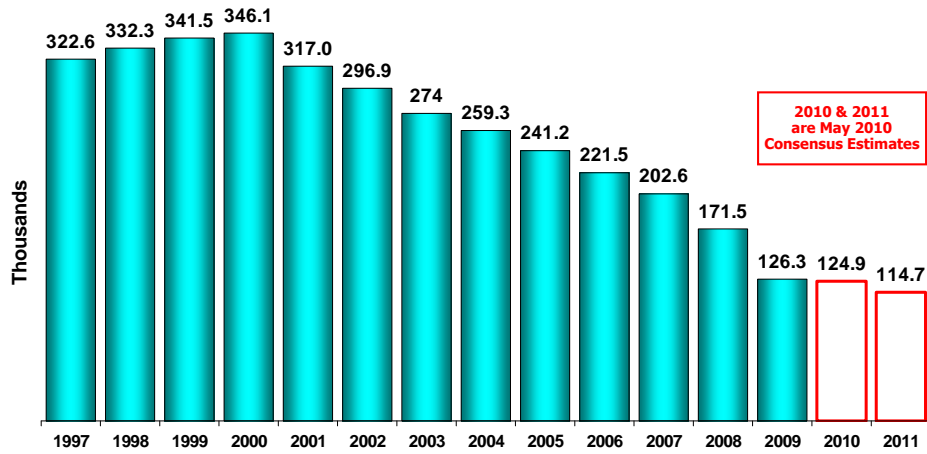


Source: Automotive News and May 2010 Consensus Estimates

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## Michigan Vehicle Employment



2010 & 2011  
are May 2010  
Consensus Estimates



Source: U.S. Bureau of Labor Statistics and May 2010 Consensus Estimates

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## Property Value Growth Slowing

### Yearly Change

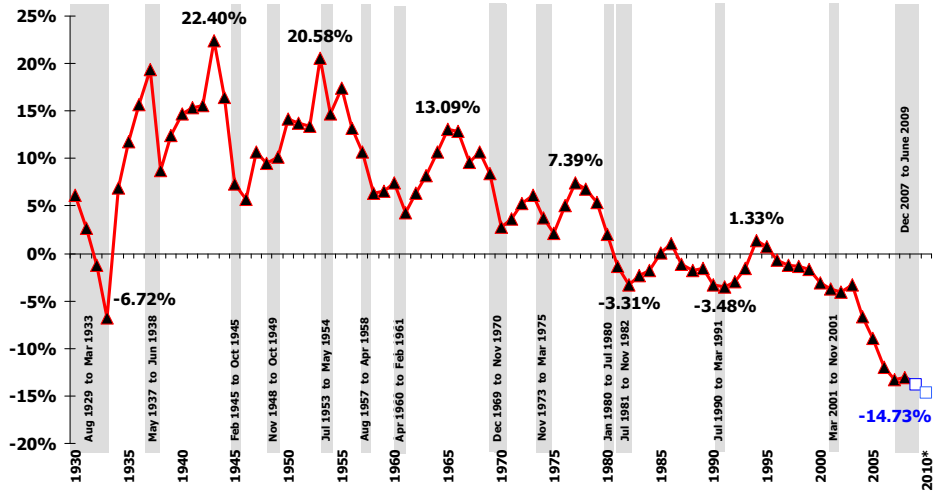
	Inflation Rate Multiplier for Property	Total SEV Growth	Total Taxable Value Growth
1997	2.8 %	8.2 %	5.7 %
1998	2.7 %	9.5 %	6.1 %
1999	1.6 %	9.9 %	6.0 %
2000	1.9 %	9.0 %	5.5 %
2001	3.2 %	10.0 %	7.1 %
2002	3.2 %	9.8 %	6.7 %
2003	1.5 %	7.5 %	4.8 %
2004	2.3 %	6.3 %	5.7 %
2005	2.3 %	5.9 %	5.6 %
2006	3.3 %	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 %	N/A	-8.0 %
2011	2.5 %	N/A	-4.3 %



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## Michigan Per Capita Income Deviation from National Average



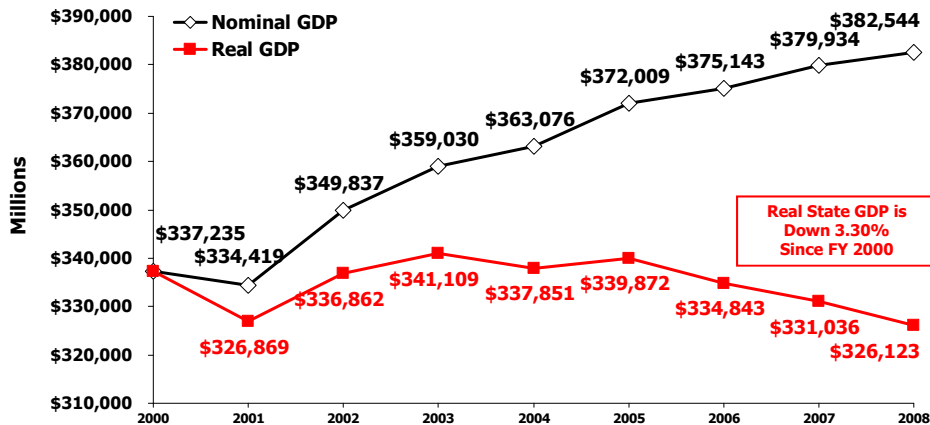
Source: National Bureau of Economic Research

\*2009 and 2010 are Estimates

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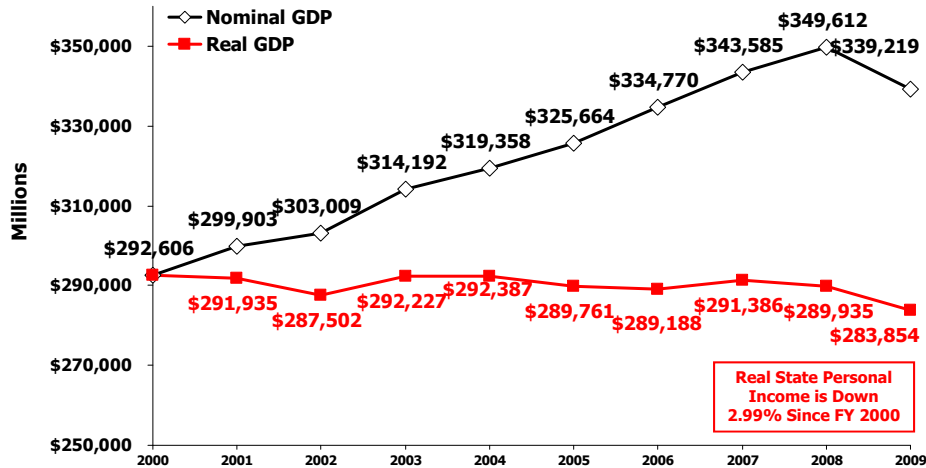
## Real and Nominal State GDP



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## Real and Nominal State Personal Income



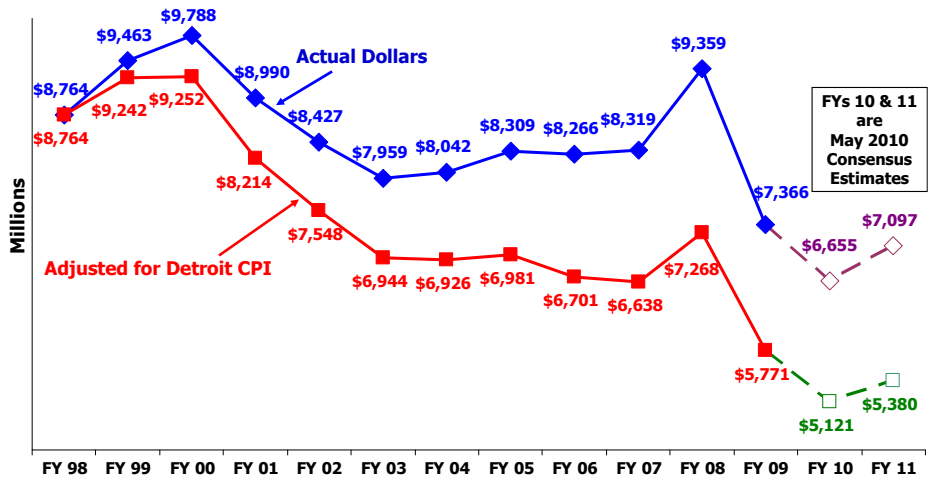
Source: U.S. Bureau of Economic Analysis. 2009 personal income numbers are from the May 2010 Consensus Revenue Estimating Conference.

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Real State Personal Income is Down 2.99% Since FY 2000



## Inflation Adjusted GF/GP Revenue Down 42% Since FY 2000

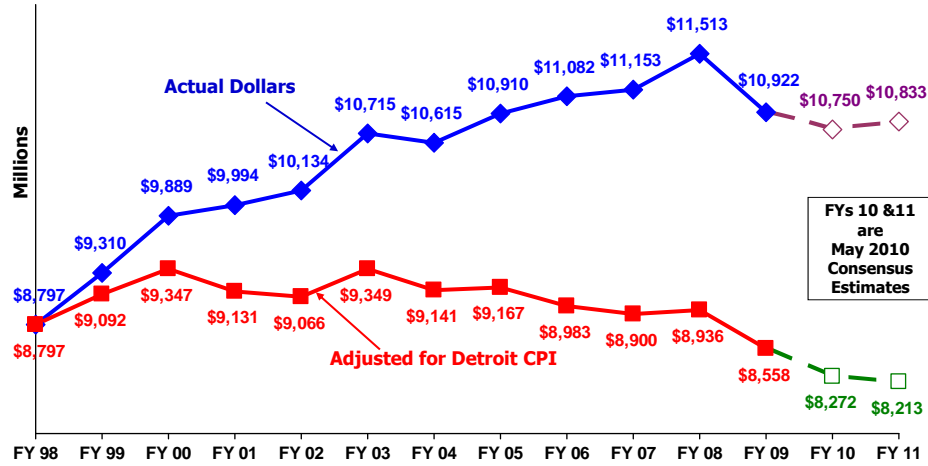


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FYs 10 & 11 are May 2010 Consensus Estimates



## Inflation Adjusted SAF Net Revenue Down 12% Since FY 2000

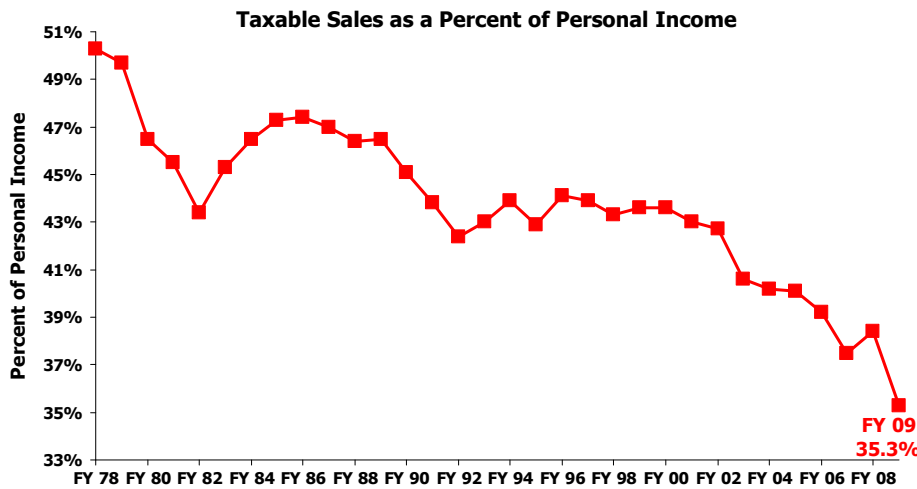


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## Sales/Use Tax Share Declining

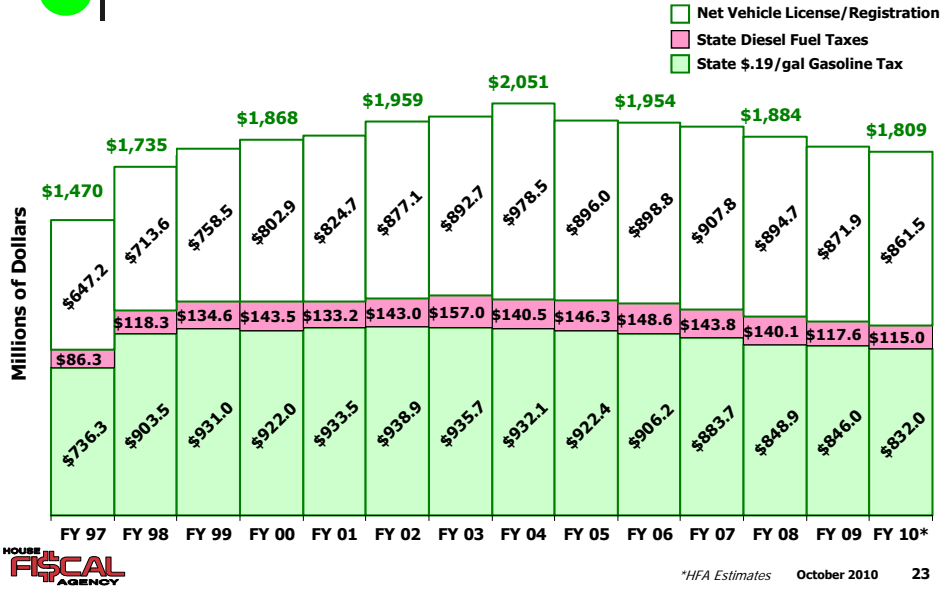


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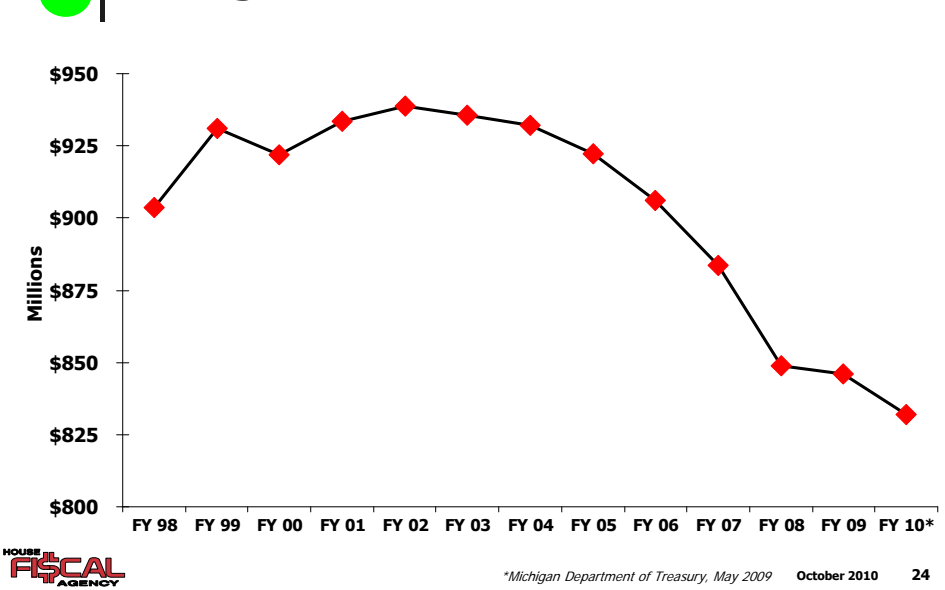
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## Transportation Revenue

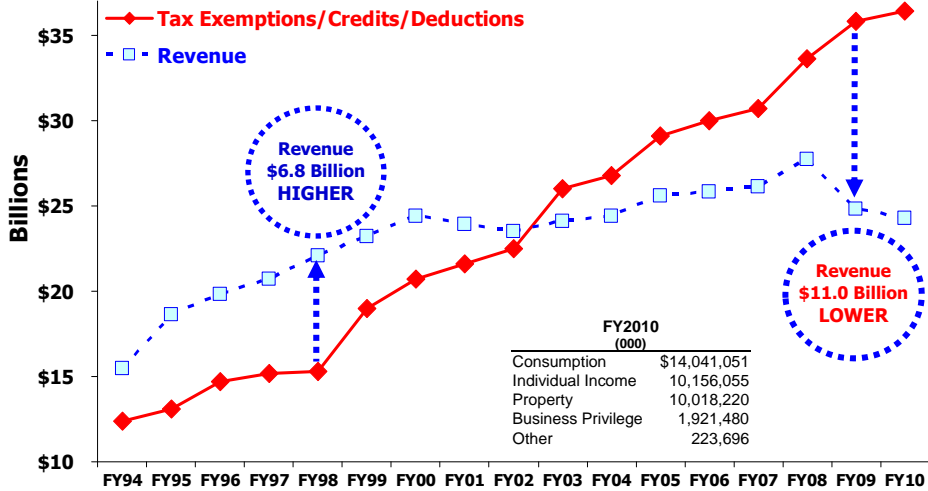


## Michigan Gasoline Tax Revenue





## Impact of Tax Exemptions/Credits/Deductions



## TAX EXPENDITURES



## 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	(\$150.0)	(\$329.0)	(\$522.5)
Alternative Energy Credits - Income Tax	(\$16.0)	(\$46.0)	(\$47.0)	(\$42.0)	\$0.0	\$0.0
Michigan EITC	(\$140.0)	(\$325.0)	(\$338.0)	(\$358.3)	(\$379.8)	(\$402.6)
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)	(\$100.0)	(\$125.0)	(\$125.0)	(\$125.0)	(\$125.0)
Photovoltaic Technology - Facility & Manufacturing	\$0.0	(\$0.8)	(\$9.8)	(\$12.5)	(\$12.5)	(\$15.0)
Polycrystalline Manufacturing Credit	\$0.0	\$0.0	\$0.0	\$0.0	(\$25.0)	(\$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)
Promise Zones - SET	\$0.0	(\$1.0)	(\$4.0)	(\$10.0)	(\$15.0)	(\$20.0)
IFT Exemption for Commercial Real Land	\$0.0	(\$2.0)	(\$2.0)	(\$2.0)	(\$2.0)	(\$2.0)
Use Tax Bad Debt Deduction Change (Court Case)	(\$2.0)	(\$25.5)	(\$16.6)	(\$17.1)	(\$17.7)	(\$18.4)
Exempt Supplies for Cobo Center	\$0.0	\$0.0	(\$2.5)	(\$2.5)	(\$3.5)	(\$1.5)
<b>Totals in Millions</b>	<b>(\$138.8)</b>	<b>(\$557.4)</b>	<b>(\$624.1)</b>	<b>(\$840.5)</b>	<b>(\$1,264.7)</b>	<b>(\$1,493.3)</b>



## Potential GF/GP Revenue Growth (millions)

	Consensus FY 2011	FY 2012	FY 2013	FY 2014
<b>Baseline Revenue</b>				
* Assume 3% Growth	\$6,968.4	\$7,177.5	\$7,392.8	\$7,614.6
<b>Adjust for Tax Change Not Built Into FY 2011</b>	N/A	(\$194.4)	(\$591.5)	(\$789.1)
<b>Net GF/GP Revenue</b>	N/A	\$6,983.1	\$6,801.3	\$6,825.5
<b>Percent Change from Prior Year</b>	N/A	0.2%	(2.6%)	0.4%

\* Note: 3% baseline growth has not been achieved since 2000.



## Selected Tax Expenditures Estimated FY2009-10 Amounts (in \$000s)

<b><u>Consumption</u></b>		<b>\$14,041,051</b>	
Services	\$10,096,211		
Food	\$1,141,588		
Industrial Processing	\$847,626		
Prescription Drugs	\$537,390		
Horticultural and Agricultural Products	\$252,880		
Residential Utilities	\$152,500	\$13,028,195	92.8%



## Selected Tax Expenditures

Estimated FY2009-10 Amounts (in \$000s)

<b><u>Property</u></b>		<b>\$10,018,200</b>	
18-mill Homestead Exemption	\$3,520,000		
Taxable Value Cap	\$3,400,000		
Tax Exempt Property	\$1,542,000		
Personal Property Tax Exemptions	\$383,100		
Industrial Facilities Development	\$256,000		
Homestead Exemption for Farm Property	\$150,000	\$9,251,100	92.3%



## Selected Tax Expenditures

Estimated FY2009-10 Amounts (in \$000s)

<b><u>Individual Income</u></b>		<b>\$10,156,055</b>	
Adjustments to Income	\$4,603,497		
Personal Exemption	\$1,165,221		
Employer Contributions to Insurance (Federal)	\$1,049,355		
Homestead Property Tax Credit	\$987,477		
Earned Income Tax Credit	\$333,000		
Social Security Deduction (Federal)	\$252,472	\$8,391,022	82.6%



## Selected Tax Expenditures

Estimated FY2009-10 Amounts (in \$000s)

<b><u>Business Privilege</u></b>		<b>\$1,921,480</b>	
Small Business Alternate Credit	\$308,100		
Compensation Credit	\$185,000		
Film Credits	\$155,100		
Personal Property Tax Credit	\$152,600		
Investment Tax Credit	\$107,400		
MEGA Credits	\$105,600	\$1,013,800	52.8%



## Senior Tax Preferences

- **Income Tax**
  - Fully exempts social security, military, federal, state and local government pension/retirement income
  - Exempts private pensions up to \$45,120 single/\$90,240 joint (TY 2009); indexed to inflation
    - Annual cost all pension income exemption = \$725 million
  - Deduction for senior investment income \$10,058 single/\$20,115 joint; indexed to inflation
    - Annual cost = \$40 - \$50 million



## Senior Tax Preferences

- **Income Tax**
  - Additional Personal Exemption \$2,300 single/\$4,600 joint (TY 2009)
  - Annual cost = \$55 million
  
- **Property Tax**
  - **Homestead Property Tax Credit**
    - Under age 65 – credit is 60% of the amount by which property taxes exceed 3.5% of household income, up to a maximum of \$1,200
    - 65 and older – credit is 100% of the difference  
Annual cost = \$320 million



## Demographics

- **Michigan's population is aging**
  - 2000 – 12.3% pop age 65+
  - 2010 – 12.8% pop age 65+
  - 2020 – 16.0% pop age 65+
  - 2030 – 19.5% pop age 65+
  
- **Senior tax preferences will get more expensive**



## Impact of Shrinking Tax Base

	<u>Income Tax Rate</u>	<u>Collections as Percent of State Personal Income</u>
<b>FY 2000</b>	<b>4.0%</b>	<b>2.6%</b>
<b>FY 2010</b>	<b>4.35%</b>	<b>1.5%</b>
<b>Revenue Impact of Declining Base</b> (In Millions of Dollars)		<b>\$3,653.50</b>
	<u>Sales and Use Tax Rate</u>	<u>Collections as Percent of State Personal Income</u>
<b>FY 2000</b>	<b>6.0%</b>	<b>2.8%</b>
<b>FY 2010</b>	<b>6.0%</b>	<b>2.1%</b>
<b>Revenue Impact of Declining Base</b> (In Millions of Dollars)		<b>\$2,511.60</b>



## Fewer People Pay Income Tax

<b><u>All Filers</u></b>	<b><u>2000</u></b>	<b><u>2008</u></b>
<b>Tax Liability &lt; \$0</b>	<b>19.5%</b>	<b>25.6%</b>
<b>Tax Liability = \$0</b>	<b>8.0%</b>	<b>8.0%</b>
<b>Tax Liability &lt; \$100</b>	<b>33.6%</b>	<b>38.6%</b>



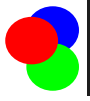
## Refundable Credits on the Michigan Income Tax

- Homestead Property Tax Credit (\$987.5 million in FY2009-10)
- Earned Income Tax Credit (\$333.0 million in FY2009-10)
- Alternative Energy/Qualified Home Improvement Credit (\$46.0 million in FY2009-10)
- Adoption Credit (\$1.0 million in FY2009-10)
- Stillbirth Credit (\$41,000 in FY2009-10)



## Indexed Provisions of the Michigan Income Tax

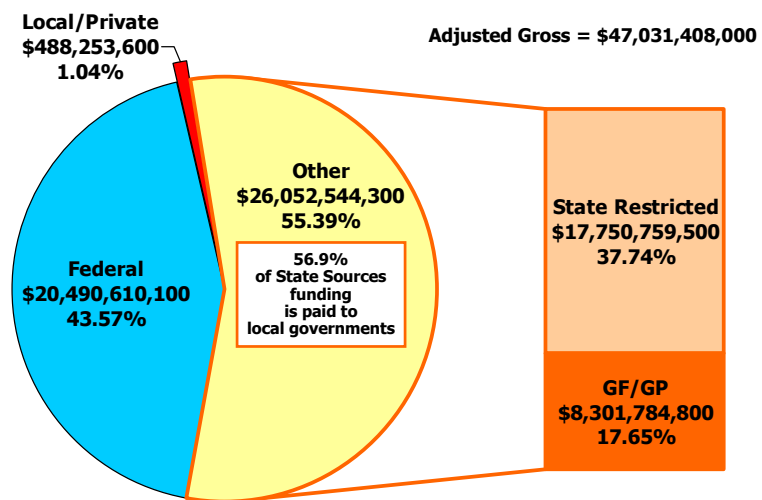
- Personal Exemption
- Special Exemptions for Seniors and/or Disabled Individuals
- Special Exemption for Qualified Disabled Veterans
- Income Threshold for Pension Income Deduction
- Income Threshold for Deduction of Interest and Capital Gains Earned by Seniors
- Home Heating Credit
- Stillbirth Credit



# MICHIGAN'S BUDGET



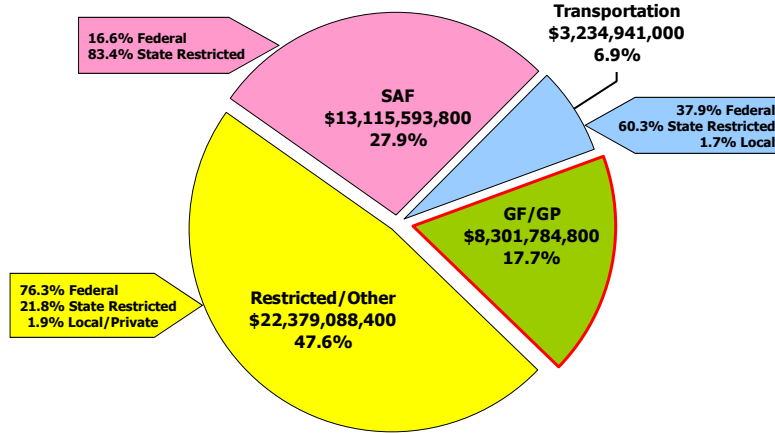
## FY 2010-11 Budget Adjusted Gross Funding Sources





## FY 2010-11 Appropriations Funding

Adjusted Gross = \$ 47,031,408,000

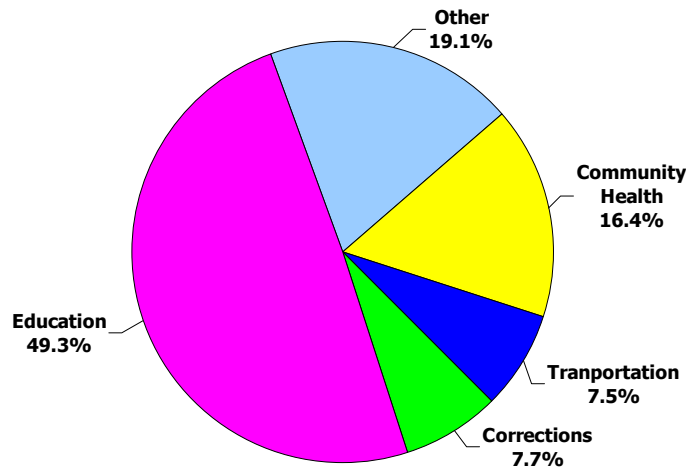


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## State Taxes and Fees FY 2010-11

FY 2010-11 Total = \$26,052,544,300

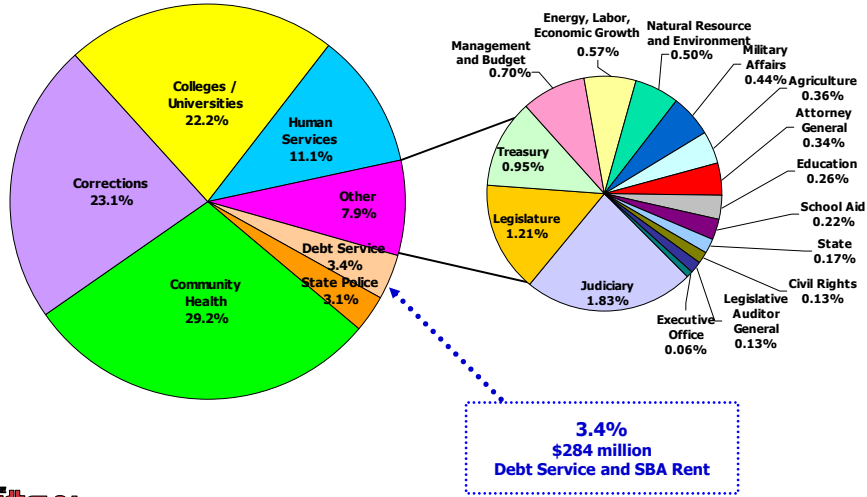


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# FY 2010-11 GF/GP

FY 2010-11 Total = \$8,301,784,800



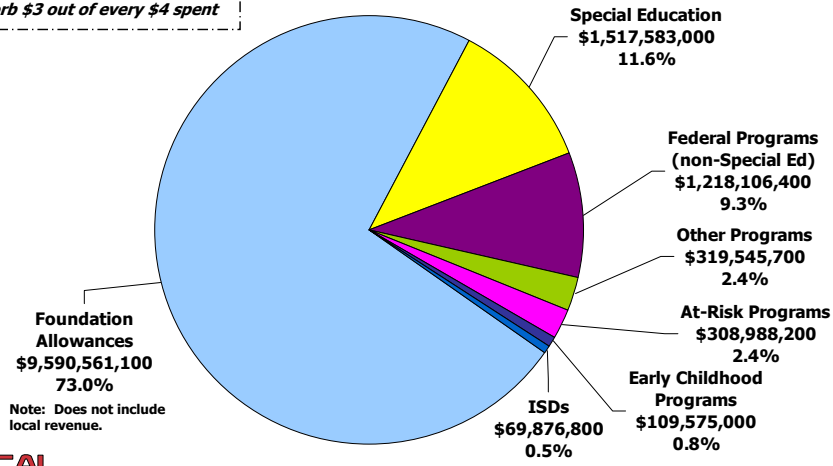
YTD 10/8/2010 October 2010 45



# 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



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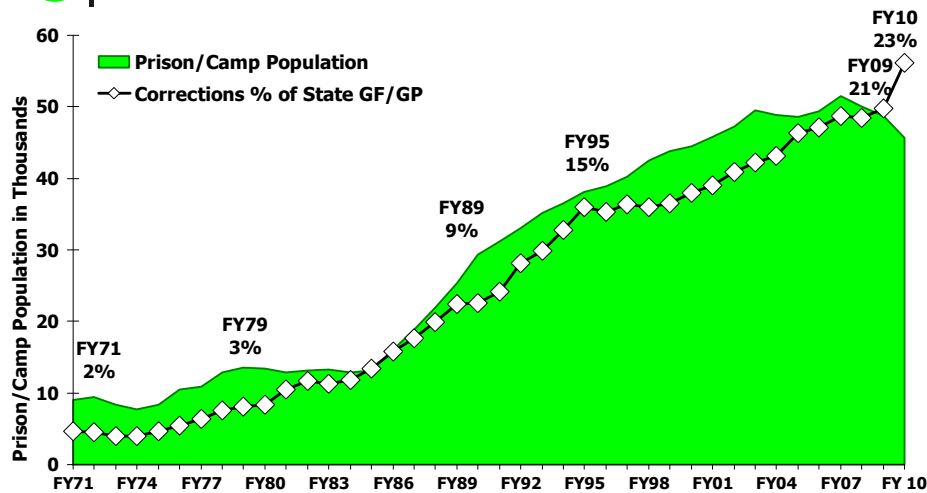


## Medicaid Impact on Michigan Budget

- For FY 10, approximately 17.7% 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 \$10.7 billion in FY 10
- Since FY 1999-2000
  - 109.8% increase in Medicaid funding
  - 52.6% growth in Medicaid caseload (559,400 cases)



## Corrections Budget Increases

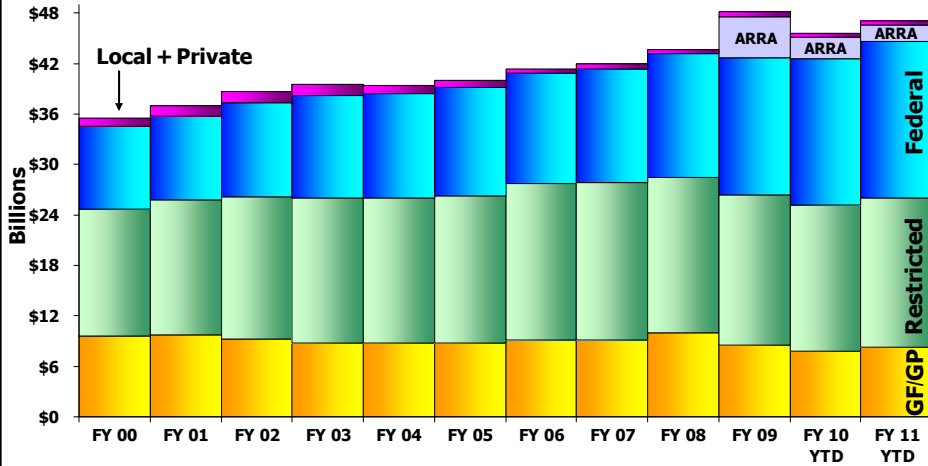


*Fiscal Year 2008-09 includes GF/GP reductions due to appropriation of federal ARRA funds.  
Fiscal Year 2009-10 includes the impact of gubernatorial vetoes of negative line items in the MDOC budget.*



## Adjusted Gross Appropriations by Fund Source

Excluding federal funds, FY 00 = FY 10 adjusted gross appropriations



Fiscal Year 2010-11 amounts include funds received under extension of temporary enhanced FMAP rate (DCH/DHS) and Ed Jobs bill (DOE/School Aid).

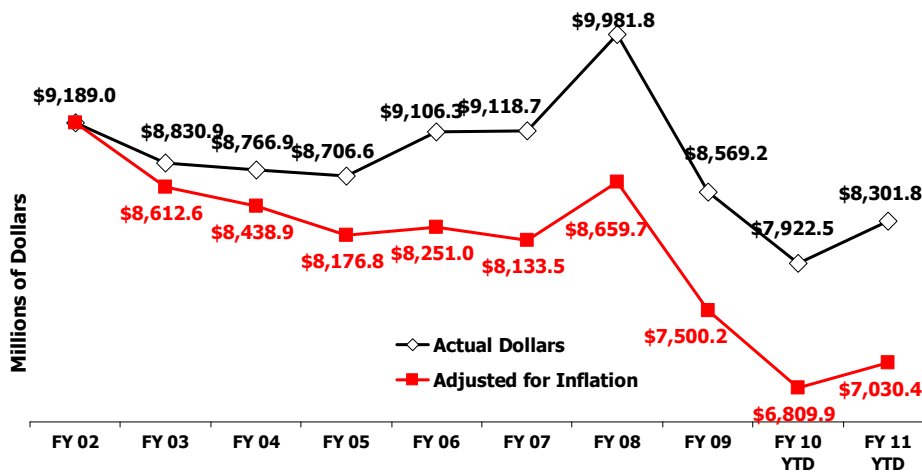
YTD 10/8/2010

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## GF/GP Appropriations



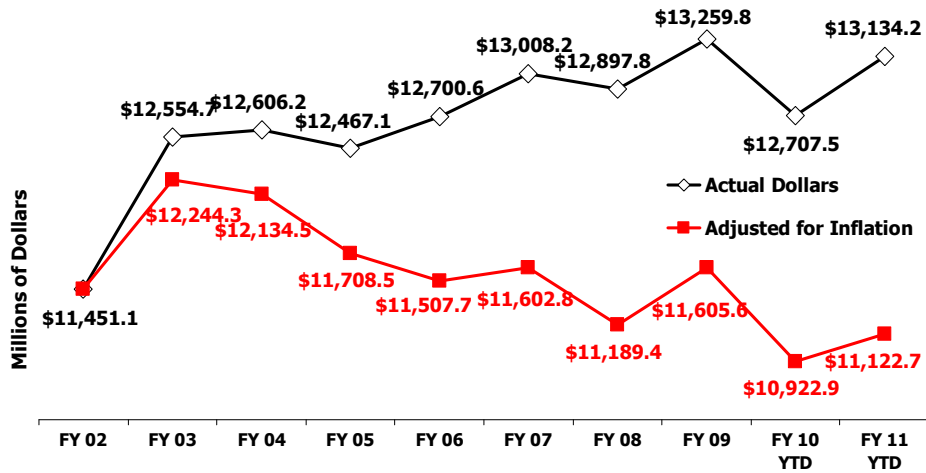
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## School Aid Budget Adjusted Gross Appropriations

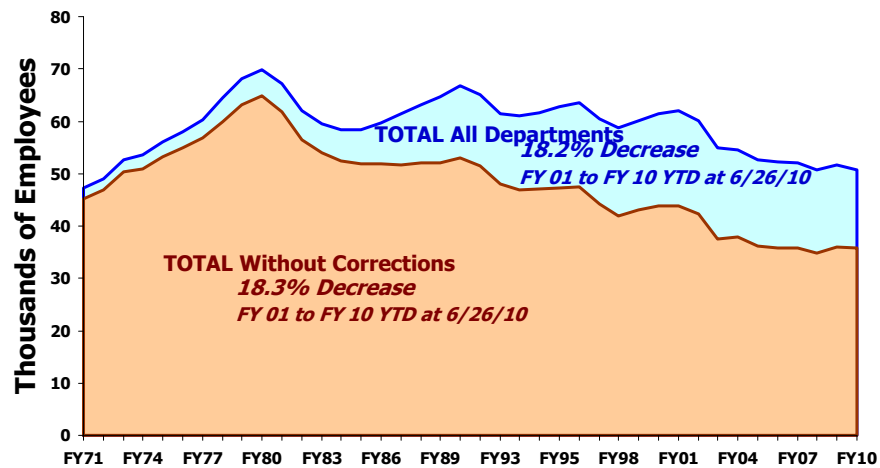


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## Average Number of Classified State Employees



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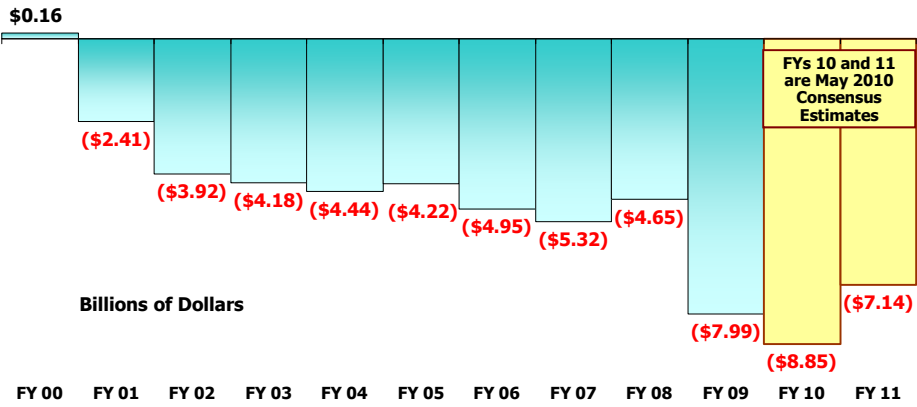
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# Constitutional Revenue Limit

Average growth of Michigan personal income = 1.7% per year from 2000 through 2011

Average decline of Michigan revenue = 0.5% per year from 2000 through 2011



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# CURRENT ISSUES



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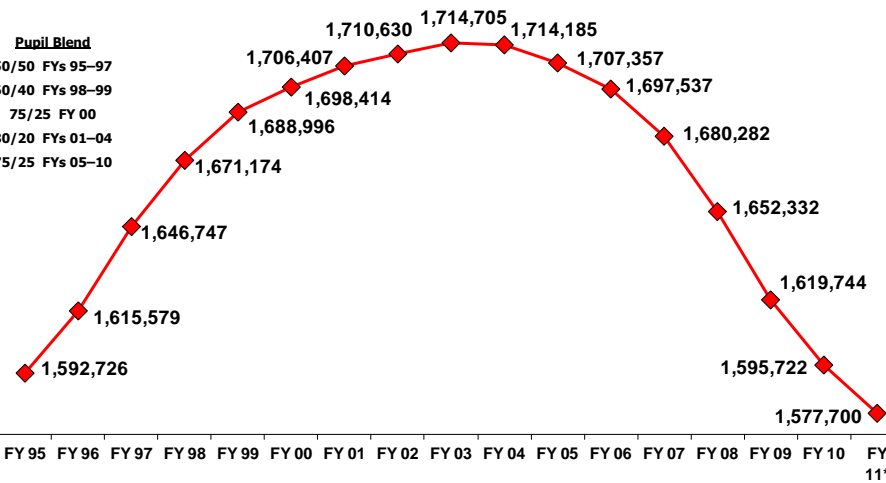
## Major School Aid Issues

- Funding levels
- Declining enrollment
- Future issues:
  - Retirement costs
  - Infrastructure financing
  - Local property taxes



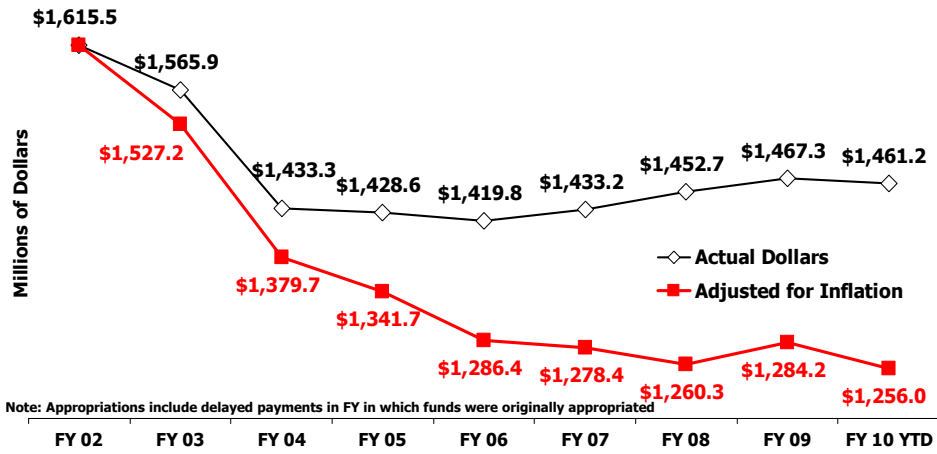
## Total Membership Pupil Counts

**Pupil Blend**  
50/50 FYs 95-97  
60/40 FYs 98-99  
75/25 FY 00  
80/20 FYs 01-04  
75/25 FYs 05-10

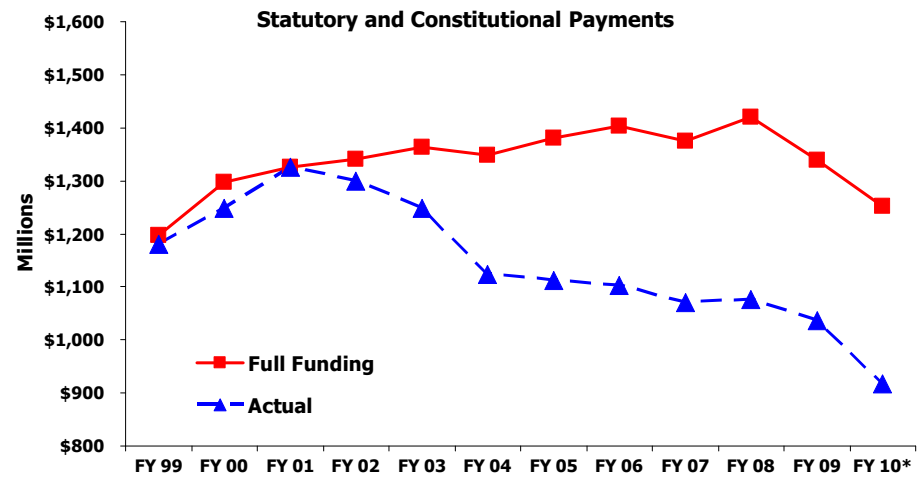




## Total Appropriations for State University Operations

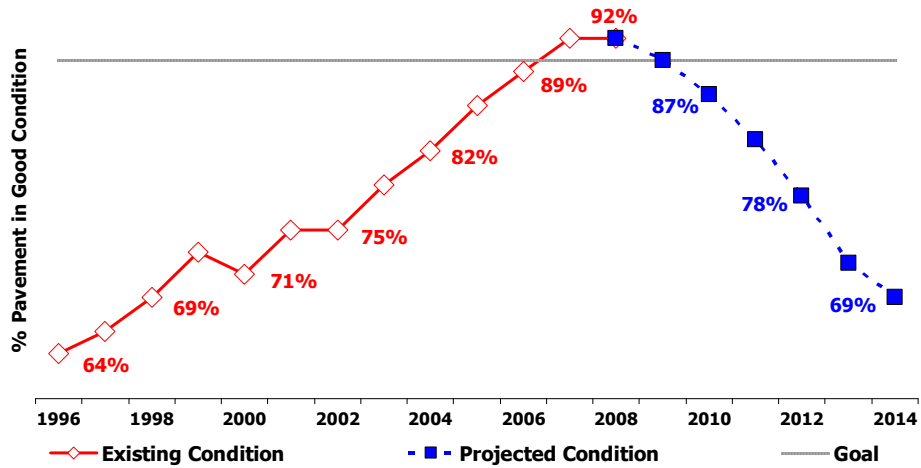


## Revenue Sharing Payments to Cities, Villages, and Townships





## Statewide Pavement Condition Combined Freeway and Non-Freeway

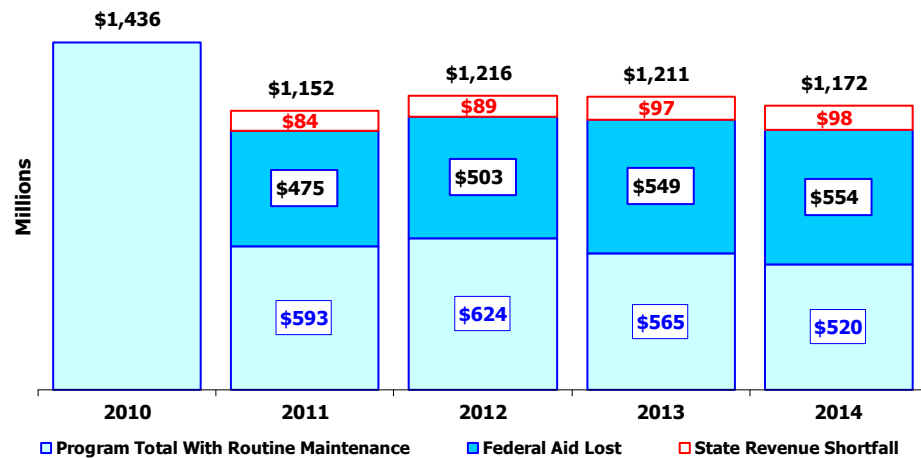


Sources: Michigan Department of Transportation website and 2010-2014 Draft Five-Year Highway Program Presentation 11/19/09

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## Reduced State Revenue May Lead to Loss of Federal Aid



Sources: Michigan Department of Transportation website and 2010-2014 Draft Five-Year Highway Program Presentation 11/19/09

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**PROBLEM: The State tax base is not stable and will not support any level of service for long.**

**SOLUTION:** Stabilize the tax base at some level – higher, lower, or revenue neutral by doing the following.

- Reduce or eliminate as many tax expenditures as possible and lower marginal rates as much as possible.
- Institute a Sunset Commission that officially reviews economic development incentives on a regular basis.
- Institute a Peer Review process using M.S.U., U of M, and the Upjohn Institute to verify the expected impact of economic development incentives.
- Institute a Pay-As-You-Go system to identify spending cuts or revenue increases to fund program expansions and new tax expenditures.

The same principles apply to a flat tax and a graduated tax. The "Best" tax system is a diverse set of taxes that are stable, simple to understand, and easy to comply with. The tax base would be as broad as possible, and marginal rates as low as possible.