

# Budget Overview

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# PRIORITIES FOR MICHIGAN'S ECONOMIC FUTURE

## *JOBS, EDUCATION AND PROTECTING FAMILIES*

### **Fiscal Year 2010 Executive Budget**

Governor Jennifer M. Granholm's 2010 Executive Budget continues the hard work of balancing limited revenues with the needs of nearly 10 million citizens feeling the impact of an economic recession. This budget is focused on the core priorities that matter most: creating jobs, educating and training our citizens and protecting families in this time of economic challenge.

Economic challenge is not new to Michigan. The state has lost more than 400,000 manufacturing jobs since this decade began as the automobile and other industries have undergone significant transformation in the face of a global economy. Consequently, Michigan has repeatedly cut spending, identified efficiencies and enacted reforms to protect critical services. A recent survey by the National Association of State Budget Officers showed that Michigan has done more since 2001 to restrain general fund spending than any state in the nation.

But the national economic collapse that began last September has added significant new complexity to an already challenged state economy. Revenues have declined sharply in subsequent months. Job losses have increased and expanded to additional sectors of the economy. And demand for state services is rising rapidly.

The result is a state budget that is impacted by both an on-going structural imbalance and a cyclical shortfall brought on by the national recession.

Further complicating the economic outlook for Michigan is the anticipation of a federal economic recovery package. While the final details of the package are not yet clear, it is reasonable to assume that Michigan will receive significant additional funding as a result. The temptation will be strong to postpone difficult budget decisions in anticipation of this additional funding, but using one-time money to fund on-going programs will only worsen our existing structural problems.

Michigan must adopt a comprehensive solution that reduces spending and implements further government reforms to ensure that we can both live within our means and use the one-time economic recovery funding as it was intended: to jumpstart the economy.

The fiscal year 2010 budget recommendation offers that comprehensive solution. It makes difficult spending cuts and identifies additional reforms. This budget enables Michigan to address our fiscal challenges directly and allows us to focus on the task of creating jobs for our citizens.

# Expectations of the Federal Economic Recovery Package

As Congress debates an economic recovery package that may put as much as \$800 billion into the national economy over the next two years to create jobs, invest in the future and help citizens who are hurting in this economic crisis, many in Michigan are understandably focused on how this package will impact our state.

Final details of this federal recovery package were not clear when this budget was constructed. While it is reasonable to assume that Michigan, like all states, would benefit from such a package, the extent of the impact is unknown.

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*“ ... shame on state leaders in Lansing if the stimulus funds deter them from doing the work they need to do to fix the state budget. A windfall from Washington is just that, a one-time thing, no matter how big.”*

**Detroit Free Press, January 24, 2009**

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More importantly, if a federal economic recovery package is adopted, it will provide only short-term stimulus funding. Extensive use of this one-time funding for on-going programs will only serve to extend the state’s structural deficit into future budget years.

Consequently, the fiscal year 2010 budget assumes only \$500 million in new revenue as a result of this economic recovery package. In addition, the fiscal year 2009 budget also assumes sufficient federal stimulus revenue to cover estimated costs. The funding for both fiscal years is expected through an increase in the federal share of funding for rising Medicaid costs.

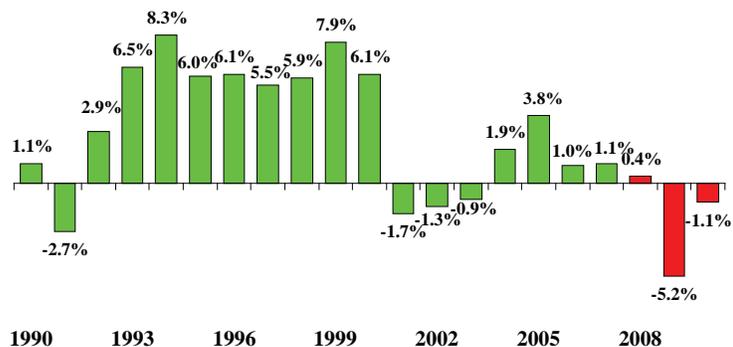
## Michigan’s Structural Deficit

Since 2001, Michigan has been unable to sustain consistent revenue growth. In four of those fiscal years, revenue growth has been negative while four more years have seen growth below the rate of inflation.

At the same time, unavoidable spending pressures have continued, including a rising prison population, increasing numbers of citizens eligible for Medicaid and additional expenses in areas such as health care and fuel.

### GF-GP and School Aid Revenue

Baseline Growth Rates Before Tax Changes



January 2009 Consensus

The result is a budget that is structurally imbalanced – where spending consistently outpaces revenues.

For the past several years, Governor Granholm has taken significant steps to address this problem.

The state has 17 percent fewer employees than it did in 2001 and employees have twice agreed to make concessions, including increased health insurance premiums and unpaid days off. In 2008, Michigan was one of only two states to provide no pay increases to its employees.

Two state departments and 156 boards and commissions have been eliminated. Department of Corrections reforms have resulted in \$460 million in savings and closure of nine facilities. Thanks in part to a successful Michigan Prisoner Reentry Initiative, the prison population is once again declining. And, additional revenue was gained through business and individual tax changes.

Despite these steps a structural deficit remains and continues to hamper efforts to invest in critical services and job creation. More must be done to address this on-going challenge.

The fiscal year 2010 Executive Budget maintains reductions contained in Executive Order 2008-21 and recommends additional spending cuts and reforms which will continue in fiscal year 2011. As noted, federal economic recovery funding used in the fiscal year 2010 budget is limited to \$500 million, which will be permanently replaced by anticipated revenue growth in 2011.

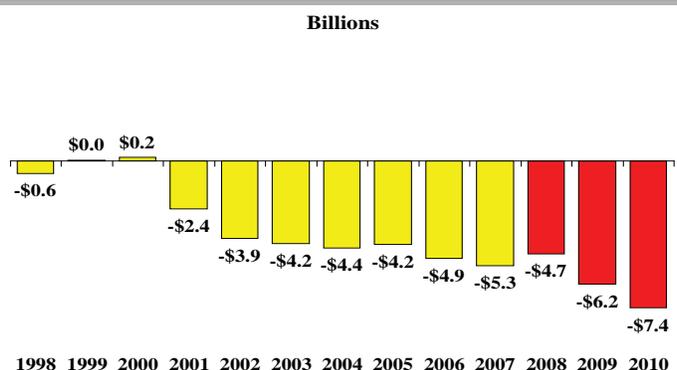
The fiscal year 2010 budget proposed today should be supported with the confidence that it offers a balanced budget for the next fiscal year and nearly eliminates the anticipated shortfall in fiscal year 2011 as well.

## Revenues

State law requires two revenue estimating conferences each year, typically held in mid-January and mid-May. Conferees include the State Treasurer and the directors of the House and Senate fiscal agencies. The conferees agree on baseline revenue estimates for the current year and the upcoming fiscal year for both the general fund and the School Aid Fund. The January conference provides revenue estimates for the Governor’s budget recommendation. The May conference provides an opportunity to revise the January estimates before final legislative action is taken on the state’s budget. Additional conferences can be held during the year if economic conditions warrant further updates to the estimates.

Like many states, Michigan has a constitutional provision that limits spending growth from year to year. Michigan’s constitutional limitation – commonly known as the Headlee

### Constitutional Revenue Limit Calculation



January 2009 Consensus

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amendment – has been in place since 1978. The Headlee amendment limits annual growth in state revenues to a level that cannot exceed the year-to-year growth in personal income. This limit is intended to ensure that the state’s overall revenues, both tax and non-tax revenues, do not grow faster than the incomes of Michigan’s citizens.

It is anticipated that state revenues for fiscal year 2010 will be \$7.4 billion below the constitutional revenue limit.

## Fiscal Year 2009 . . . Where We Stand

Despite conservative revenue estimates at the May 2008 Consensus Revenue Estimating Conference, the precipitous national economic decline that began in September 2008 has had a significant impact on state revenue collections.

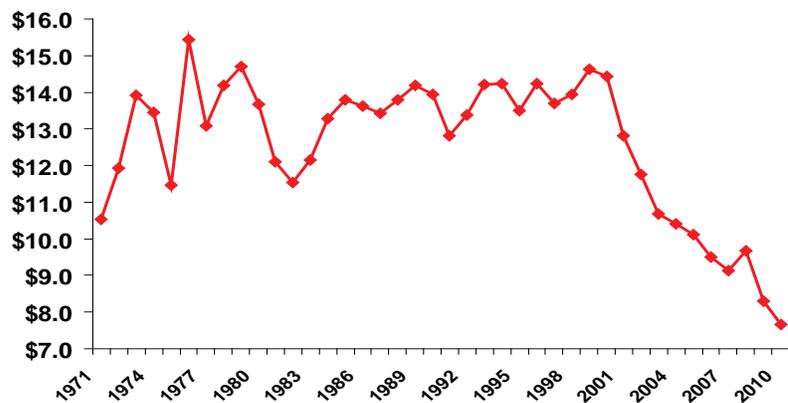
Consequently, the January 2009 Consensus Revenue Estimating Conference projected that general fund revenue for the current fiscal year will be \$8.31 billion, a reduction of \$578 million or 11.3 percent from the estimate used to construct this year’s budget.

Additionally, the Consensus Revenue Estimating Conference projected a decline in School Aid Fund revenue for the current year. Revenues are expected to be \$339 million below previous estimates in this fund.

As a result of the fast-growing national recession, state revenue estimates have declined by nearly \$1 billion for the current year, and are below 1971 levels.

The state closed its books for fiscal year 2008 with a larger budget surplus than was originally anticipated. The \$458 million surplus in the general fund and \$247 million surplus in the School Aid Fund were the result of higher than expected revenue collections in the final months of the fiscal year and spending restraint by state departments. The combined carryforward helps to partially off-set the revenue decline for the current fiscal year.

**GF-GP Revenue Below 1971 Level  
Adjusted for Inflation**  
(GF-GP Revenue in Billions of 2009 \$)



Notes: FY 2009 and FY 2010 are the January 2009 Consensus estimates. Inflation adjusted using State and Local Government Price Deflator.

Governor Granholm issued Executive Order 2008-21 on December 10, 2008 to reduce fiscal year 2009 general fund expenditures by \$134 million. This Executive Order was approved by the House and Senate Appropriations Committees on the day it was issued. After the carryforward and Executive Order cuts are considered, the remaining fiscal year 2009 funding gap is \$269 million in the general fund and \$44 million in the School Aid Fund.

This budget anticipates that the state will receive one-time federal money through an increase in the Federal Medical Assistance Percentage (FMAP) rate this year that appropriately offsets this deficit due to the cyclical downturn in the economy.

## The Fiscal Year 2010 Executive Budget Recommendation

Michigan will enter fiscal year 2010 in a time of on-going economic challenge. Like every state, the national recession is expected to continue to impact Michigan's economy and revenue collections for some time. Despite six years of budget challenges, more difficult decisions are required to balance the upcoming budget while protecting our shared priorities.

The January Consensus Revenue Estimating Conference projected revenues will be \$7.93 billion for the general fund and \$11.30 billion for the School Aid Fund.

As a result of declining revenue projections, additional debt service and spending pressures in the Departments of Corrections, Community Health and Human Services, the fiscal year 2010 budget begins with a combined general fund and School Aid funding gap of \$1.4 billion.

<b>Fiscal Year 2010 Revenue and Spending</b>			
<b>(\$ in millions)</b>			
	<b>GF/GP</b>	<b>School Aid Fund</b>	<b>Combined</b>
Consensus Revenues	\$7,935	\$11,296	\$19,230
Revenue Sharing Savings	\$467	\$0	\$467
Use Tax - 2008 PA 440	\$335	\$0	\$335
Enacted Revenue Changes	\$36	\$41	\$76
Federal Aid to Schools	\$0	\$1,562	\$1,562
<b>Total Revenue Estimate</b>	<b>\$8,772</b>	<b>\$12,898</b>	<b>\$21,670</b>
FY 09 Current Law Spending	\$9,568	\$13,379	\$22,946
Baseline Spending Adjustments			
Corrections Prison Increases	\$34	\$0	\$34
Community Health - 2008 PA 440	\$294	\$0	\$294
Community Health/Human Services Baseline	\$205	\$0	\$205
Federal Matching Rate Adjustments	(\$259)	\$0	(\$259)
Employee Economics	\$75	\$0	\$75
Revised Cost Estimates	\$0	(\$251)	(\$251)
Other Adjustments	\$21	\$0	\$21
<b>Total Baseline Spending Estimate</b>	<b>\$9,938</b>	<b>\$13,128</b>	<b>\$23,066</b>
<b>Projected Funding Gap</b>	<b>(\$1,166)</b>	<b>(\$229)</b>	<b>(\$1,396)</b>
Proposed Revenue Adjustments	\$166	\$65	\$232
Spending Reductions and Reforms	\$506	\$164	\$670
Federal - Enhanced FMAP	\$500	\$0	\$500
<b>Total FY 2010 Funding Surplus</b>	<b>\$6</b>	<b>\$0</b>	<b>\$6</b>

To address this shortfall, Governor Granholm is proposing additional government reforms and spending cuts.

First, the Governor's budget builds on efforts over the last several years to reduce costs through restructuring, streamlining and other efficiencies. Savings are achieved in this budget through several different types of governmental reforms, including:

- Closure of state-operated facilities, including:
  - Several additional correctional facilities,
  - the Department of Community Health's Mount Pleasant Center for persons with developmental disabilities, transferring the patients to community care settings, as appropriate,
  - the Maxey Woodland Training Center, transferring youth offenders to a smaller, more cost effective facility on the Maxey campus, and
  - the Michigan State Police crime lab in Marquette.
- Elimination of state support for non-core functions or functions that can be done by other entities, including:
  - ending financial support for the state fairs in Detroit and the Upper Peninsula,
  - eliminating supplemental financial support for the horse racing industry,
  - returning responsibility for wetlands protections to the federal Environmental Protection Agency.
- Streamlining government operations by:
  - overhauling the state's higher education scholarship programs to create a single merit-based scholarship - Michigan Promise Grants - and a single needs - based scholarship - Michigan College Access Grants - open to all students attending public or private institutions,
  - combining the Cooperative Extension Service and Agricultural Experiment Station,
  - consolidating energy programs in the Department of Energy, Labor and Economic Growth.
- Administrative reforms, including:
  - eliminating the Department of History, Arts and Libraries,
  - opening a one-stop-shop for business - a simple web portal to put hundreds of business transactions seamlessly on-line.
  - seeking employee concessions.

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*" Governor Jennifer Granholm and the Legislature should make sure strategies for dealing with ongoing deficits are structural solutions that position the state for economic growth."*

**Grand Rapids Press, January 16, 2009**

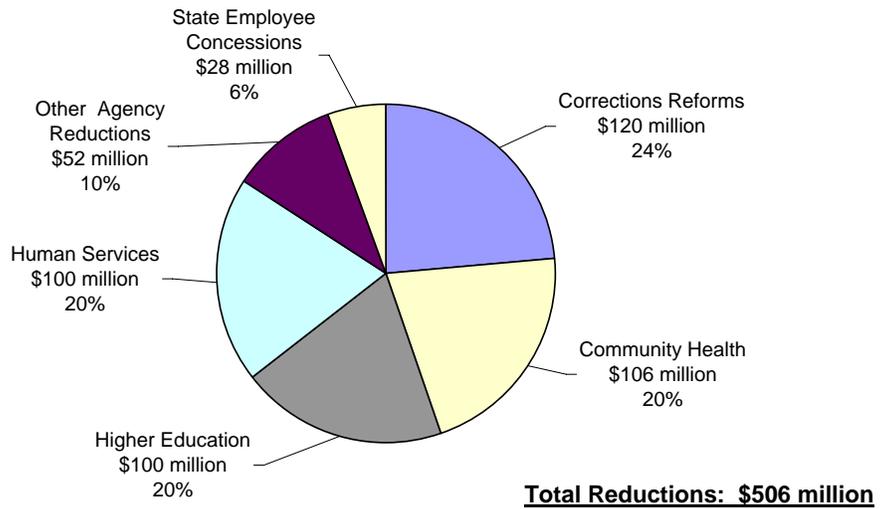
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- Investment in community-based services:
  - additional investment in community-based monitoring for parolees,
  - accelerating transition of seniors and the disabled from nursing homes to community care settings.

Second, the Governor proposes \$670 million in spending reductions, impacting every state department. These cuts would be permanent and on-going. They include:

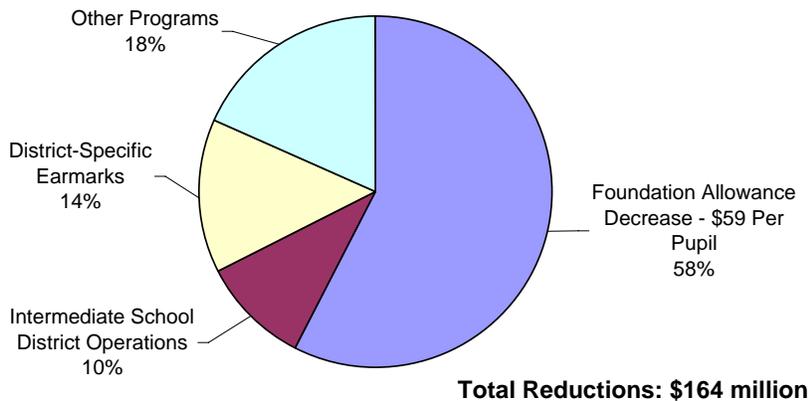
- Elimination of \$50 million in earmarks, including pilot programs and programs which serve single school districts, communities or regions,
- \$106 million in cuts in the Department of Community Health, including reductions in the Office of Services to the Aging, elimination of the Office of Drug Control Policy and changes in prescription drug purchasing,
- \$100 million in cuts in the Department of Human Services, including eliminating before and after school programs and the supplemental payment for Supplemental Security Income recipients,
- \$164 million in cuts to K-12 spending which includes a reduction in the per-pupil foundation allowance of \$59 per student, and
- \$100 million in cuts to higher education funding, including a three percent reduction to university operations.

**Fiscal Year 2010 General Fund Reductions**



- \$100 million in cuts in the Department of Human Services, including eliminating before and after school programs and the supplemental payment for Supplemental Security Income recipients,
- \$164 million in cuts to K-12 spending which includes a reduction in the per-pupil foundation allowance of \$59 per student, and
- \$100 million in cuts to higher education funding, including a three percent reduction to university operations.

**Fiscal Year 2010 School Aid Reductions**



As a result of the cuts and reforms proposed, more than 1,500 state employee positions will be eliminated in fiscal years 2009 and 2010.

Finally, the 2010 Executive Budget Recommendation includes \$230 million in additional revenue as a result of tax loophole closures, increased liquor license fees and permit revenues, lottery investments and tax enforcement actions.

# Protecting our Shared Priorities

In addition to the spending cuts and additional reforms offered in this year's Executive Recommendation, the Governor's proposed budget continues critical investments in priority areas.

## JOB CREATION, EDUCATION AND TRAINING

During this time of economic challenge, job creation is the single-most important priority of the Granholm administration and the Governor's fiscal year 2010 budget reflects that commitment. Funding for No Worker Left Behind is maintained and federal funding will be used to create the Michigan Energy Corps to put thousands of unemployed citizens back to work this year.

Despite painful cuts to many areas of the budget, funding for community colleges, which play a critical role in these expanded worker training programs, is maintained.

The 21st Century Jobs Fund will continue to support job creation in growing economic sectors including renewable energy, life sciences, homeland security and advanced manufacturing.

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*"Michigan will weather this economic storm because our people are resourceful and resilient and because our battle plan is focused on the three things that matter most: fighting for more good paying jobs in Michigan; educating and training our people to fill those jobs; and protecting our families."*

**Governor Granholm, State of the State Message,  
February 3, 2009**

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The newly-reorganized Department of Energy, Labor and Economic Growth will provide over \$123 million for energy programs and regulation, including streamlined energy efficiency programs within the new Bureau of Energy Systems.

## PROTECTING FAMILIES

Despite significant economic challenges over the last six years, Governor Granholm has consistently supported protecting critical health care programs for vulnerable citizens. This year's budget recommendation continues that commitment.

Funding for Medicaid is increased to over \$11 billion to support an increased demand for health care services. In addition, health care coverage will be expanded to 4,000 disabled children at no additional state cost and additional community-based service options for seniors and the disabled will both save money and improve care.

The Governor's budget proposal continues the state's commitment to strengthening Michigan's child welfare system by investing an additional \$113 million to hire child protective services workers, expand the foster care staff and increase capacity to manage adoptions.

This budget recommendation also continues to expand investments in the state's unemployment insurance system including hiring additional staff to handle the significant increase in need.

Governor Granholm's 2010 budget also recommends:

- More than \$84 million for food safety and consumer protection programs,
- \$171 million for environmental clean-up and pollution prevention programs,
- nearly \$54 million to protect citizens through regulation of the insurance and mortgage industries,
- increased funding for the Michigan State Police to cover costs associated with assuming responsibility for the Detroit Crime Lab, and
- continued revenue sharing support for local government services including police and fire protection.

## Conclusion

This is a time of unprecedented challenge for the entire nation and Michigan is feeling the impact. To ensure that we emerge from this period a stronger, more nimble, more financially stable state will require focus, discipline and a willingness to make tough decisions.

Governor Granholm's fiscal year 2010 Executive Budget Recommendation is a critical component in achieving that goal. It offers the fiscal discipline that is required to address the state's on-going structural deficit, while continuing to provide the essential services that are needed to help citizens weather the current economic storm.