

**SENATE FISCAL AGENCY  
 MEMORANDUM**

**DATE:** October 21, 2010  
**TO:** Members of the Senate  
**FROM:** Gary S. Olson, Director  
**RE:** FY 2011-12 State Budget Outlook

On January 1, 2011, a newly elected Michigan Governor will begin the task of developing a State budget recommendation for the fiscal year beginning on October 1, 2011. Pursuant to statutory requirements, the new Governor will have to submit a detailed FY 2011-12 State budget recommendation to the Legislature by March 6, 2011. This State budget recommendation by the Governor will begin legislative debate on the FY 2011-12 State budget.

The parameters of the FY 2011-12 State budget recommendation of the Governor are not known today. What is known is that due to a variety of factors related to the enacted FY 2010-11 State budget, the new Governor and the newly elected members of the Legislature will face difficult decisions in developing and enacting the FY 2011-12 State budget. This is especially true when examining the issues surrounding the FY 2011-12 General Fund/General Purpose (GF/GP) budget.

The following information provides the Senate Fiscal Agency (SFA) outlook for both the FY 2011-12 GF/GP and School Aid Fund budgets.

**Fiscal Year 2011-12 General Fund/General Purpose Budget Outlook**

The enacted FY 2010-11 GF/GP budget is balanced with a combination of temporary Federal funds, nonrecurring revenue from several statutory changes and appropriation reductions. It is now the belief of the SFA that the temporary Federal funds that were such an important part of balancing the FY 2008-09, FY 2009-10, and FY 2010-11 GF/GP budgets will not be available in FY 2011-12. This assumption is based on the belief that the United States Congress is unlikely to continue the temporary emergency Federal aid to states that has occurred over the past three fiscal years.

On the revenue side of the FY 2011-12 GF/GP budget, two factors will have an impact on the level of revenue available to support expenditures. The first is that several nonrecurring revenue sources were used to balance the FY 2010-11 GF/GP budget. The second is that under current law, the rate of the State income tax will decline from 4.35% to 4.25% on October 1, 2011.

The combination of the assumed elimination of the temporary Federal aid and these revenue changes will lead to a significant challenge in ensuring a balance between FY 2011-12 GF/GP revenue and appropriations. Table 1 provides a summary of the FY 2011-12 GF/GP budget outlook. The SFA is estimating a \$1.4 billion imbalance between potential GF/GP revenue and appropriations. This imbalance equals 16.9% of the level of FY 2010-11 GF/GP appropriations.

**Table 1**  
**FY 2011-12 State Budget Outlook**  
**General Fund/General Purpose Budget**  
**(Millions of Dollars)**

<b>Revenue</b>	
FY 2010-11 GF/GP Revenue Base .....	\$8,252.8
<b>Revenue Adjustments:</b>	
Unclaimed Property Changes .....	(91.0)
Tax Amnesty .....	(91.7)
Convention Facility Fund Transfer .....	(5.0)
Secretary of State Work Project Transfer .....	(6.0)
Increased County Revenue Sharing Payments .....	(37.3)
Income Tax Rate Reduction (October 1, 2011) .....	(150.0)
Subtotal One-Time Revenue Adjustments .....	(381.0)
Adjusted FY 2010-11 GF/GP Revenue Base .....	\$7,871.8
Assume 4.0% Revenue Growth .....	314.9
<b>Net FY 2011-12 GF/GP Revenue .....</b>	<b>\$8,186.7</b>
<b>Appropriations</b>	
FY 2010-11 Enacted GF/GP Appropriations .....	\$8,230.0
<b>FY 2011-12 Appropriation Adjustments:</b>	
Enhanced Medicaid Match Rate .....	520.0
Human Services Emergency TANF Funds .....	239.0
Medicaid One-Time VEBA Payment .....	160.0
Medicaid Caseload/Costs .....	210.0
Federal Medicaid Match Rate .....	(35.0)
Human Services Caseload/Costs/Full Year Staffing Levels .....	91.0
General Obligation Bond Debt Restructuring .....	83.3
State Police One-Time Revenue Adjustments .....	5.8
State Employee Economic Costs .....	103.7
Subtotal Funding Adjustments .....	1,377.8
<b>Adjusted FY 2011-12 GF/GP Appropriation Base .....</b>	<b>\$9,607.8</b>
<b>Potential Funding Imbalance .....</b>	<b>\$(1,421.1)</b>

The SFA's FY 2011-12 GF/GP budget outlook assumes total GF/GP revenue of \$8.2 billion. This estimate is developed using the current estimate of FY 2010-11 GF/GP revenue as a base and adjusting for nonrecurring revenue items and the change in the income tax rate. These nonrecurring revenue items included revenue from changes in the State accounting of unclaimed property, revenue from a tax amnesty program, State restricted revenue transfers to the GF/GP budget, and the additional GF/GP revenue impact of increased revenue sharing payments to counties. The final assumption regarding the FY 2011-12 GF/GP revenue base is an assumed 4.0% growth in GF/GP revenue. The actual level of FY 2011-12 GF/GP revenue growth will be determined when the Consensus Revenue Estimating Conference establishes the initial estimate of FY 2011-12 GF/GP revenue in January 2011.

The SFA's FY 2011-12 GF/GP budget outlook assumes total GF/GP appropriations of \$9.6 billion. This estimate is developed using the FY 2010-11 enacted appropriations as the starting point. Adjustments then are made for temporary Federal funds in the Community Health and Human Services budgets that will not be available in FY 2011-12. These adjustments total \$919.0 million. Assumptions are also made concerning caseload and cost growth in the Medicaid program offset partially by an increase in Michigan's ongoing Federal Medicaid match rate.

Additional expenditures in the Human Services budget are a result of caseload, full-year staffing, and cost increases. Funding adjustments are also included for the additional costs of debt service on General Obligation bonds resulting from restructuring changes made during FY 2010-11. The final expenditure adjustments include the elimination of one-time funding sources in the State Police budget and projected increases in State employee costs. These projected increases in State employee costs include health insurance costs, retirement costs, and changes in the level of savings from the recently enacted policy changes in the State Employees Retirement System.

This SFA outlook on the FY 2011-12 GF/GP budget is built on freezing the funding in FY 2011-12 at the FY 2010-11 levels for such programs as revenue sharing payments to cities, villages, and townships, aid to universities and community colleges, and a general freeze in other grant programs. The assumptions also assume no changes in State tax laws outside of the already-enacted reduction in the rate of the State income tax.

In summary, the newly elected Governor and the members of the Legislature will face significant challenges in enacting a balanced FY 2011-12 GF/GP budget. In many respects, the challenge in passing a balanced FY 2011-12 GF/GP budget would have occurred in FY 2008-09, FY 2009-10, and FY 2010-11 if the United States Congress had not provided Michigan with approximately \$3.1 billion of temporary Federal funds that helped eliminate many of the difficult budget decisions. The anticipated elimination of these temporary Federal funds will mean the fundamental decisions regarding the future of the GF/GP budget will be made during FY 2011-12.

### **Fiscal Year 2011-12 School Aid Fund Budget Outlook**

While the newly elected Governor and the Legislature will face significant challenges in developing a FY 2011-12 GF/GP budget the outlook regarding the FY 2011-12 School Aid Fund budget is much better. This difference is based on a smaller reliance on temporary Federal funds in the School Aid budget and the fact that the impact of the enacted income tax rate reduction affects only the GF/GP budget and not the School Aid Fund budget.

The factors influencing the outlook for the FY 2011-12 School Aid Fund budget include projected revenue growth, the loss of temporary Federal funds, debt service funding increases and continued projections for a decline in the number of students. Table 2 provides a summary of the FY 2011-12 School Aid Fund budget outlook. The SFA is estimating a \$103.7 million imbalance between potential School Aid Fund revenue and appropriations.

The SFA's FY 2011-12 School Aid Fund budget outlook assumes total School Aid Fund revenue of \$13.1 billion. This estimate is developed using the current consensus estimate of FY 2010-11 School Aid Fund revenue and adjusting for nonrecurring revenue items. These nonrecurring revenue items include \$184.3 million of temporary Federal funding related to the American Recovery and Reinvestment Act of 2009 and \$316.3 million of temporary Federal funding related to the Education Jobs Act of 2010. Additional nonrecurring revenue items include revenue related to tax amnesty and the spend down of projected balances from the prior fiscal year. The final assumptions regarding the FY 2011-12 School Aid Fund revenue base is an assumed 4.0% growth in ongoing School Aid Fund revenue and a freeze in the ongoing level of Federal revenue. The actual level of FY 2011-12 School Aid Fund revenue will be determined when the Consensus Revenue Estimating Conference establishes the initial estimate of FY 2011-12 School Aid Fund revenue in January 2011.

**Table 2**  
**FY 2011-12 State Budget Outlook**  
**School Aid Fund**  
**(Millions of Dollars)**

<b>Revenue</b>	
FY 2010-11 School Aid Fund Revenue Base .....	\$11,549.7
Ongoing Federal Funds.....	1,677.8
<b>Revenue Adjustments:</b>	
Federal ARRA Funding .....	(184.3)
Federal Education Jobs Funding .....	(316.3)
Tax Amnesty .....	(26.1)
Drawdown of Beginning Balance .....	<u>(70.0)</u>
Subtotal One-Time Revenue Items .....	(596.7)
Adjusted FY 2010-11 SAF Revenue Base .....	\$12,630.8
Assume 4.0% Revenue Growth .....	438.1
<b>FY 2011-12 SAF Revenue Base .....</b>	<b>\$13,068.9</b>
<b>Appropriations</b>	
Enacted FY 2010-11 Appropriations .....	\$13,134.2
<b>FY 2011-12 Appropriation Adjustments:</b>	
Reduction in Spending Related to Pupil Counts .....	(90.0)
School Bond Loan Fund Debt Service Adjustment.....	88.4
Special Education Cost Increase .....	<u>40.0</u>
Subtotal Appropriation Adjustments .....	38.4
<b>Adjusted FY 2011-12 SAF Appropriation Base .....</b>	<b>\$13,172.6</b>
<b>Potential Funding Imbalance .....</b>	<b>\$(103.7)</b>

The SFA's FY 2011-12 School Aid Fund budget outlook assumes total School Aid Fund appropriations of \$13.2 billion. This estimate is developed using the enacted level of FY 2010-11 appropriations. Adjustments then are made for a projected decline in the number of students to be funded and funding increases related to debt service payments and special education costs. These appropriation assumptions mean that local school districts will continue to receive the level of per-pupil funding that they are receiving in the current fiscal year, after the Legislature completes action on the appropriation of new Federal funds related to the Education Jobs Act of 2010.

The projected \$103.7 million funding imbalance in the FY 2011-12 School Aid Fund budget equals 0.2% of FY 2010-11 School Aid Fund appropriations. In summary, the newly elected Governor and the members of the Legislature will likely be able to provide some sort of continuation funding for local school districts in FY 2011-12 based on the assumptions outlined in this analysis.

/kjh

c: Ellen Jeffries, Deputy Director  
 SFA Fiscal Analysts