

# State Notes

## TOPICS OF LEGISLATIVE INTEREST

### July/August 2003



#### **Balancing the State General Fund/General Purpose Budget: Three Consecutive Years of Fiscal Stress**

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The slowing of the United States and Michigan economies, which began in the spring of 2000, ended up having a very significant impact on state budgets. The economic slowdown, coupled with a massive drop in the valuation of equity stocks, resulted in actual state revenue collections' falling under the initial estimates on which state appropriations were based. This decline in state revenue collections forced most states to institute significant changes in their state budgets from the point that original spending plans were recommended by state Governors until the final revenue and expenditure totals were reached at the close of the states' fiscal years.

This article provides a summary of the steps that were taken by the Michigan Governor and the Legislature to adjust the State's General Fund/General Purpose (GF/GP) budget from the original recommendation of the Governor to the final revenue and expenditure totals. The analysis covers fiscal years 2000-01, 2001-02, and 2002-03, the three recent fiscal years most affected by the deteriorating economic conditions.

The Michigan budget process begins in the winter before the start of the State's next fiscal year, when the Governor, pursuant to constitutional and statutory requirements, delivers a detailed budget recommendation to the Legislature. This budget recommendation includes any recommended tax policy changes along with a comprehensive set of recommended appropriations for each State department or agency. The Governor's budget recommendation sets off a budget process that concludes at the end of the fiscal year when the final accounting of actual State revenues and expenditures is completed.

In order to analyze the changes in the Michigan GF/GP budget from the original recommendation of the Governor to the final revenue and expenditure figures, the following assumptions are used. A comparison of the Governor's original GF/GP appropriation recommendation to the final level of GF/GP ongoing revenues is undertaken. The difference between these two numbers is the amount of deficit that the Governor and the Legislature were forced to eliminate throughout the fiscal year in order to keep the GF/GP budget in balance. This analysis will explain in each of the three fiscal years how much of this deficit was eliminated as a result of reductions in appropriations from the Governor's original recommendation versus tax policy changes that increased revenues above the amount assumed in the Governor's original budget versus other policy changes that had the impact of providing increased GF/GP revenues to support appropriations.

#### **Fiscal Year 2000-01 GF/GP Budget**

On January 27, 2000, Governor John Engler presented to the Legislature his recommendation for the fiscal year (FY) 2000-01 GF/GP budget. The Governor recommended GF/GP appropriations of \$9.64 billion. When the final accounting of FY 2000-01 GF/GP revenues was completed, the amount of ongoing GF/GP revenues actually collected totaled \$8.99 billion, for an imbalance of \$647.9 million from the Governor's original appropriation recommendation.

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Table 1 provides a summary of the actions that the Governor and the Legislature took to eliminate this imbalance.

<b>Table 1</b> <b>FY 2000-01 General Fund/General Purpose Budget Summary</b> <b>Governor's Original Proposal to Final Bookclosing</b> <b>(millions of dollars)</b>	
Governor's Original Appropriation Recommendation . . . . .	\$9,637.4
Final Consensus Revenue Collections . . . . .	8,989.5
Difference . . . . .	\$ (647.9)
 <u>Actions Taken to Balance Budget:</u>	
GF/GP Appropriation Increases . . . . .	(79.1)
 <u>Non-Ongoing Revenue Sources:</u>	
Budget Stabilization Fund Withdrawal . . . . .	270.0
Use of Prior Year-End Balance . . . . .	211.8
Tobacco Settlement Trust Fund Transfer . . . . .	20.0
State Building Authority Funding Shift . . . . .	211.2
Work Project Reductions . . . . .	42.1
Subtotal Non-Ongoing Revenue Adjustments . . . . .	<u>\$755.1</u>
<b>Remaining Balance . . . . .</b>	<b>\$ 28.1</b>

In terms of appropriations, the actual level of FY 2000-01 GF/GP expenditures exceeded the level originally recommended by the Governor by \$79.1 million. The imbalance was closed by a variety of actions that provided for non-ongoing increases in GF/GP revenues. These revenue increases included a \$270.1 million withdrawal from the Budget Stabilization Fund, the use of a \$211.8 million beginning balance carried forward from FY 1999-2000, a \$211.2 million funding shift in the construction of new State-financed buildings from a cash system of financing to debt issued by the State Building Authority, a \$20.0 million transfer of Tobacco Settlement Trust Fund revenue, and \$42.1 million of revenue from the liquidation of several prior work project accounts. These actions in total eliminated the imbalance and allowed FY 2000-01 to close with a \$28.1 million balance.

**Fiscal Year 2001-02 GF/GP Budget**

On February 8, 2001, Governor Engler presented to the Legislature his recommendation for the FY 2001-02 GF/GP budget. The Governor recommended GF/GP appropriations of \$9.78 billion. When the final accounting of FY 2001-02 GF/GP revenues was completed, the amount of ongoing GF/GP revenues actually collected totaled \$8.28 billion, for an imbalance of \$1.51 billion from the Governor's original appropriation recommendation. Table 2 provides a summary of the actions that the Governor and the Legislature took to eliminate this imbalance.

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<b>Table 2</b>	
<b>FY 2001-02 General Fund/General Purpose Budget Summary</b>	
<b>Governor's Recommendation to Final Bookclosing</b>	
<b>(millions of dollars)</b>	
Governor's Original Appropriation Recommendation . . . . .	\$9,784.6
Final Consensus Revenue Collections . . . . .	8,276.2
Difference . . . . .	\$(1,508.4)
<u>Actions Taken to Balance Budget:</u>	
GF/GP Appropriation Reductions	662.5
<u>Non-Ongoing Revenue Sources:</u>	
Budget Stabilization Fund Withdrawal . . . . .	452.8
Use of Prior Year-End Balance . . . . .	28.1
Merit Award Trust Fund Transfers . . . . .	131.5
Tobacco Settlement Trust Fund Transfers . . . . .	27.5
Revenue Sharing Reductions . . . . .	60.5
Employment Contingency Fund Transfer . . . . .	79.5
Transportation Funding Shifts . . . . .	63.0
Homestead Property Tax Credit to TANF . . . . .	56.0
Tax Amnesty Revenue . . . . .	15.5
Work Project Reductions . . . . .	28.7
Other Revenue/Fund Shift Adjustments . . . . .	17.3
Total Adjustments to Balance Budget . . . . .	\$1,622.9
<b>Actual Year-End Balance . . . . .</b>	<b>\$ 114.5</b>

In terms of appropriations, the actual level of FY 2001-02 GF/GP appropriations was \$662.5 million below the level originally recommended by the Governor. The remaining amount of the \$1.51 billion imbalance was closed by non-ongoing GF/GP revenue increases. These revenue increases included a \$452.8 million withdrawal from the Budget Stabilization Fund, the use of a \$28.1 million beginning balance carried forward from FY 2000-01, a \$131.5 million transfer from the Merit Award Trust Fund, a \$27.5 million transfer from the Tobacco Settlement Trust Fund, a \$60.5 million revenue increase from a reduction in the statutory level of revenue sharing payments, a \$79.5 million transfer from the Employment Contingency Fund, a \$63.0 million transfer from statutory restricted transportation funds, a \$56.0 million revenue increase from the shifting of the financing of homestead property tax credits to available Federal funds, a \$15.5 million revenue increase from a tax amnesty program, a \$28.7 million revenue increase from the liquidation of several prior year work project accounts, and \$17.3 million from other fund shifts and revenue adjustments. These actions in total eliminated the imbalance and allowed FY 2001-02 to close with a \$114.5 million balance.



**Fiscal Year 2002-03 GF/GP Budget**

On February 7, 2002, Governor Engler presented to the Legislature his recommendation for the FY 2002-03 GF/GP budget. The Governor recommended GF/GP appropriations of \$9.29 billion. The current consensus estimate of FY 2002-03 ongoing GF/GP revenues is \$7.87 billion, for an imbalance of \$1.42 billion from the Governor's original appropriation recommendation. Table 3 provides a summary of the actions that Governor Engler, Governor Jennifer Granholm and the Legislature took to eliminate this imbalance.

<b>Table 3</b>	
<b>FY 2002-03 General Fund/General Purpose Budget Summary</b>	
<b>Governor's Original Proposal to Current Enacted Budget</b>	
<b>(millions of dollars)</b>	
Governor's Original Appropriation Recommendation . . . . .	\$ 9,285.3
May 2003 SFA Consensus Revenue Estimate . . . . .	7,865.9
Difference . . . . .	\$(1,419.4)
<u>Actions Taken to Balance Budget:</u>	
GF/GP Appropriation Reductions . . . . .	478.3
<u>Revenue Increases:</u>	
Tobacco Tax Increase . . . . .	141.6
Pause in Single Business Tax Rollback . . . . .	76.3
Subtotal Revenue Increases . . . . .	217.9
<u>Other Non-Ongoing Revenue Sources:</u>	
Budget Stabilization Fund Withdrawal . . . . .	115.1
Use of Prior Year-End Balance . . . . .	114.5
Merit Award Trust Fund Transfer . . . . .	151.3
Tobacco Settlement Trust Fund Transfer . . . . .	14.6
Revenue Sharing Reductions . . . . .	146.2
Revenue Sharing Reserve Account . . . . .	195.6
Unrestricted Federal Aid . . . . .	169.0
Sale of Surplus Property . . . . .	69.5
SERS Pre-Funded Health Reserve . . . . .	58.2
Liquor Purchase Revolving Fund Transfer . . . . .	3.7
Waterways Fund Transfer . . . . .	7.8
Hospital Assessment Revenue . . . . .	8.9
Investor Lawsuit Settlement . . . . .	14.3
Vitamin Lawsuit Settlement . . . . .	10.1
Tobacco Company Lawsuit Settlement . . . . .	7.0
Federal Tax Reform State Revenue Impact . . . . .	(7.1)
Federal Unemployment Benefits Extension(Income Tax) . . . . .	5.1
Subtotal Non-Ongoing Revenue Sources . . . . .	<u>\$1,083.8</u>
Total Actions Taken to Balance Budget . . . . .	<u>\$1,780.0</u>
<b>Remaining Balance . . . . .</b>	<b>\$360.6</b>



During the summer of 2002, the Legislature, as a result of a recommendation from Governor Engler, took two actions dealing with tax policy to address this imbalance. The rate of the excise tax on cigarettes was increased from 75 cents per pack to \$1.25 per pack. A portion of this revenue increase totaling \$141.6 million was dedicated to the GF/GP budget. The other tax policy change implemented at this time was a suspension of the 0.1 percentage point reduction in the rate of the Single Business Tax scheduled to occur on January 1, 2003. This suspension of the Single Business Tax rate reduction resulted in a \$76.3 million increase in FY 2002-03 GF/GP revenue.

In terms of appropriations, the year-to-date level of FY 2002-03 GF/GP appropriations is \$478.3 million below the level originally recommended by the Governor. The remaining amount of the \$1.42 billion imbalance was closed by non-ongoing GF/GP revenue increases. These revenue increases included a \$115.1 million transfer from the Budget Stabilization Fund, the use of a \$114.5 million beginning balance carried forward from FY 2001-02, a \$151.3 million transfer from the Merit Award Trust Fund, a \$14.6 million transfer from the Tobacco Settlement Trust Fund, \$146.2 million from a reduction in the statutory level of revenue sharing payments, \$195.6 million from the transfer of a revenue sharing reserve account, \$169.0 million from unrestricted Federal funds, \$69.5 million from the sale of surplus State property, \$58.2 million from a transfer from the State Employees Retirement System, and a variety of other non-ongoing revenue items that increased revenues by \$49.8 million. These actions in total eliminated the imbalance and will allow the FY 2003-03 GF/GP budget to close with a \$360.6 million balance.

### **Summary**

During the past three fiscal years, the Michigan GF/GP budget has faced a total of \$3.58 billion in projected imbalances between the Governor's original appropriation recommendation and the final level of ongoing GF/GP revenue collections. [Table 4](#) provides a summary of the actions that were taken over this three-fiscal-year period to eliminate these budget imbalances. Appropriation reductions over the period totaled \$1.16 billion or 26.0% of the total adjustments taken to eliminate the imbalances. Other actions taken to eliminate these projected imbalances included transfers from the Budget Stabilization Fund, \$837.9 million or 20.5% of the total adjustments; the use of prior year-end balances, \$354.4 million or 8.7% of the total adjustments; transfers from tobacco settlement funds, \$344.9 million or 8.5% of the total adjustments; revenue increases, \$217.9 million or 5.3% of the total adjustments; State revenue sharing reductions, \$206.7 million or 5.1% of the total adjustments; a transfer from the revenue sharing reserve, \$195.6 million or 4.8% of the total adjustments; unrestricted Federal aid, \$169.0 million or 4.1% of the total adjustments; and \$479.0 million of other adjustments, or 11.7% of the total adjustments.

It is clear that the Governor and the Legislature have used a wide array of fiscal changes in order to keep the GF/GP budget in balance over the past three fiscal years. The use of these fiscal adjustments is important to an understanding of how the budget has been balanced and also provides a source of budget-balancing ideas that could be used in future economic downturns.

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<b>Table 4</b>					
<b>Actions Taken to Balance GF/GP Budgets</b>					
<b>(millions of dollars)</b>					
	<b>FY</b>	<b>FY</b>	<b>FY</b>	<b>Total</b>	<b>% of</b>
	<b>2000-01</b>	<b>2001-02</b>	<b>2002-03</b>		<b>Total</b>
Potential Deficit . . . . .	\$(647.9)	\$(1,508.4)	\$(1,419.4)	\$(3,575.7)	—
Appropriation Reductions	(79.1)	662.5	478.3	1,061.7	26.0%
Budget Stabilization Fund Transfers	270.0	452.8	115.1	837.9	20.5%
Use of Prior Year-End Balance	211.8	28.1	114.5	354.4	8.7%
Tobacco Settlement Transfers	20.0	159.0	165.9	344.9	8.5%
Revenue Increases	0.0	0.0	217.9	217.9	5.3%
State Building Authority Fund Shift	211.2	0.0	0.0	211.2	5.2%
Revenue Sharing Statutory Reductions	0.0	60.5	146.2	206.7	5.1%
Revenue Sharing Reserve Transfer	0.0	0.0	195.6	195.6	4.8%
Unrestricted Federal Aid	0.0	0.0	169.0	169.0	4.1%
All Other Fund Shifts/Transfers	42.1	260.0	176.9	479.0	11.7%
Total Adjustments	<u>\$676.0</u>	<u>\$1,622.9</u>	<u>\$1,779.4</u>	<u>\$4,078.3</u>	100.0%
<b>Year-End Balance . . . . .</b>	<b><u>\$28.1</u></b>	<b><u>\$114.5</u></b>	<b><u>\$360.0</u></b>		