

State Notes

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An Assessment of the Principal Cost Growth in the Michigan Department of Corrections By John Maxwell, Fiscal Analyst

In 2010, the Senate Fiscal Agency examined the cost drivers of the Michigan Department of Corrections (MDOC) budget from fiscal year (FY) 2000-01 through FY 2008-09. In that analysis, an effort was made to reconcile a declining prison population and MDOC full-time equated positions (FTEs) with an overall increased appropriation figure. The analysis identified two trends that explained some of the reasons for a declining prison population without a corresponding drop in budget appropriations: employee economic costs and prisoner health care expenditures. This report will update the data with five years of additional data to determine whether those trends are still apparent in the MDOC budget.

Trends in MDOC Appropriations

Tables 1 and 2 reflect the changes that have occurred over the 10-year history of MDOC appropriations and year-end prison population between FY 2005-06 and FY 2014-15. Table 1 shows that since FY 2006-07, there has been a consistent decline in the number of FTEs while the Gross appropriations have been more uneven. The Gross appropriations include Federal and Restricted funds as well as General Fund/General Purpose (GF/GP) revenue. Despite the inconsistent nature of the Gross appropriations, the GF/GP appropriations have increased year over year since FY 2011-12. Over the 10-year period of appropriations between FY 2005-06 and FY 2014-15, Gross appropriations have increased nearly \$155.0 million in nominal terms while GF/GP appropriations have increased nearly \$175.0 million in nominal terms, leading to an increased GF/GP portion of the budget.

Table 1

Department of Corrections Funding History					
Fiscal Year	Full-Time Equated Positions (FTEs)	Year-to-Date Gross Appropriation	Year-to-Date GF/GP Appropriation	% Change in Gross Appropriation	% Change in GF/GP Appropriation
FY 2005-06	17,509	\$1,885,554,200	\$1,806,098,500	1.1%	5.4%
FY 2006-07	17,782	1,953,623,000	1,871,877,500	3.6	3.6
FY 2007-08	17,637	2,079,681,100	1,996,084,500	6.5	6.6
FY 2008-09	17,285	2,038,478,100	1,778,041,400	(2.0)	(10.9)
FY 2009-10	16,005	1,999,606,600	1,919,711,100	(1.9)	8.0
FY 2010-11	15,878	1,991,313,500	1,900,078,400	(0.4)	(1.0)
FY 2011-12	15,569	1,990,534,400	1,921,594,300	0.0	1.1
FY 2012-13	14,758	2,021,915,600	1,941,235,600	1.6	1.0
FY 2013-14	14,560	2,047,106,400	1,972,725,400	1.2	1.6
FY 2014-15	14,179	2,040,521,700	1,980,798,400	(0.3)	0.4

Source: Annual Year-to-Date Appropriations Acts

As Table 2 shows, after five consecutive years of prisoner population decreases from 2007 to 2011, the population has rebounded to an extent and has seemingly plateaued at an average of between 43,000 and 44,000 prisoners.

The number of people committed to prison increased to over 10,000 in 2013. This represents an increase of about 400 over 2012. Notwithstanding the nearly 8,000-prisoner decrease from the peak in 2006, the appropriations have stayed relatively constant.



Table 2

Prison Population Figures			
Calendar Year	Year-End Population	Numerical Change	Percent Change
2004	48,557	330	N/A
2005	49,377	820	1.7%
2006	51,454	2,077	4.2
2007	50,203	(1,251)	(2.4)
2008	48,686	(1,517)	(3.0)
2009	45,478	(3,208)	(6.6)
2010	44,113	(1,365)	(3.0)
2011	42,904	(1,209)	(2.7)
2012	43,594	690	1.6
2013	43,704	110	0.3
2014 ^{a)}	43,414	(290)	(0.7)

^{a)} Population number taken from FY 2014-15 appropriation bill, Public Act 252 of 2014.

Source: MDOC Annual Statistical Report

MDOC Employee Expenditures

As the budget has remained at consistent levels even as the Department has experienced changes in the number of prisoners, the workforce has become an area with a greater impact on the MDOC appropriation. According to the FY 2013-14 MDOC spending plan¹, of the \$2,039,605,800 budget for Department operations, \$816,348,100 went to State employee wages and \$672,279,500 went to State employee benefits. The total salary and wage expenditure of \$1,488,627,600 makes up 73% of the MDOC spending plan. Though Table 1 shows a decrease in FTEs and Table 2 shows a decline in prisoner population, the increase in the appropriation over the 10-year period is partially explained by changes in employee economics. These changes in economics have been necessitated by the demographic trends among MDOC employees as well as modifications to State employment benefits and the provision of funds for unfunded accrued liabilities for Other Post-Employment Benefits (OPEB) rather than on a "pay-as-you-go" basis. In FY 2003-04, the average age of the employees was 43.4 years, the average length of service was 12.1 years, and the average hourly pay was \$21.54². In the second quarter of FY 2013-14, the average age of MDOC employees was 45.8 years, the average length of service was 14.6 years, and the average hourly pay was \$25.77³. Even as the employee workforce has shrunk, the simple demographic shift toward an older, more experienced workforce has resulted in an increase in economic expenditures. Compared with the other State departments, the MDOC has the second-highest percentage of employees eligible for longevity pay, at 80.7%⁴. Additionally, due to the older makeup of the MDOC workforce, there has been an increase in the number of sick days taken by the MDOC employees: in FY 2003-04, the MDOC had an average of 11.5 sick days (92.0 hours) per employee while in FY 2012-13, the average was 13.01 sick days (104.1 hours) taken. Table 3 reflects that, even with a decline in prison population as well as FTEs, the employee economics have increased in keeping with the contracted terms of employment.

¹ MDOC Spending Plan FY 2013-14

² FY 2003-04 Civil Service Workforce Report

³ FY 2013-14 2nd Quarter Michigan Civil Service Workforce Report

⁴ Id

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Table 3

History of Employee-Related Economic Increases								
Fiscal Year	Salary	Insurance	Retirement	OPEB	Worker's Compensation	Other	Total Change in Employee Economics	Total Departmentwide Appropriation Increase
2002-03	\$17,876,300	\$0	\$2,331,800		\$1,365,600	(\$7,217,100) ^{a)}	\$14,356,600	\$17,854,300
2003-04 ^{b)}	0	0	0		2,823,000	28,595,600 ^{c)}	112,628,900	37,450,369
2004-05	61,617,600	21,209,900	68,827,200		(2,549,000)	(46,342,500) ^{d)}	102,763,200	80,352,719
2005-06	10,590,700	22,831,700	18,362,900		(1,378,000)	46,342,500 ^{d)}	96,749,800	91,198,600
2006-07	36,328,100	13,633,100	32,057,900		(1,105,000)	0	80,914,100	54,867,300
2007-08	41,987,300	16,612,500	24,272,600		(932,000)	0	81,940,400	124,646,100
2008-09	10,004,600	(12,298,700)	7,320,000		(533,000)	0	4,492,900	(39,032,900)
2009-10	9,411,900	6,807,300	15,206,400		473,000	0	31,898,600	(54,869,300)
2010-11	27,236,600	18,810,200	37,169,500	0	1,822,000	0	85,038,300	(8,293,100)
2011-12	0	(6,563,100)	62,857,700	0	126,100	0	56,420,700	(779,100)
2012-13	24,591,300	(9,864,600)	(88,938,100)	\$121,618,700	2,284,600	0	49,691,900	31,381,200
2013-14	7,905,500	3,139,300	30,120,600	6,670,200	852,800	0	48,688,400	25,190,800
2014-15 ^{e)}	14,552,800	0	16,850,200	(8,198,800)	(1,447,900)	0	21,756,300	(6,584,700)

^{a)} This eliminated a lump sum salary payment that had been part of the contract during FY 2000-01 and FY 2001-02.
^{b)} Salary, insurances, and retirement increases were unfunded this year, but totaled \$81.2 million.
^{c)} Restored FY 2002-03 shortfalls in retirement.
^{d)} This reduction and subsequent increase of the same amount marked the start and end of employee concessions such as furlough days and banked leave time.
^{e)} Based on FY 2014-15 initial appropriations.

Source: State Budget Office



Prisoner Health Care Costs

Along with an aging workforce, the "silver tsunami" has hit the prisoner population as well. As [Table 4](#) shows, both the average age and the median age of the prisoners have gone up since 2000. More importantly, however, the share of those prisoners over the age of 55 has increased substantially. In 2000, less than 5% of the overall population was over 55, but by 2013, the share was nearly 12%. This represents an increase of 138% over the 13-year period. More than one out of every 10 prisoners is over the age of 55.

Table 4

Prisoner Age Data					
Calendar Year	Total Population	Prisoners' Average Age	Prisoners' Median Age	Prisoners Age 55+	% of Prisoners 55+
2000	47,718	35.1	34	2,107	4.4%
2001	48,849	35.4	34	2,365	4.8
2002	50,591	35.6	34	2,674	5.3
2003	49,357	35.9	35	2,865	5.8
2004	48,831	36.3	35	3,096	6.3
2005	49,139	36.6	36	3,370	6.9
2006	51,515	36.9	36	3,760	7.3
2007	50,233	37.2	36	4,021	8.0
2008	48,713	38.0	37	4,662	9.6
2009	45,478	38.0	37	4,217	9.3
2010	44,113	38.0	36	4,145	9.4
2011	42,904	38.0	36	4,318	10.1
2012	43,594	38.0	37	4,712	10.8
2013	43,704	38.0	37	5,013	11.5

Source: Annual MDOC Statistical Report

Table 5

Prisoner Health Care Appropriations History			
Fiscal Year	MDOC Gross Appropriation	Health Care Gross Appropriation¹⁾	Health Care as a % of Gross Appropriation
1999-2000	1,564,700,800	120,151,100	7.7%
2000-01	1,706,276,900	140,086,100	8.2
2001-02	1,688,016,300	148,907,800	8.8
2002-03	1,687,056,831	156,308,800	9.3
2003-04	1,705,829,881	162,015,700	9.5
2004-05	1,768,907,800	170,036,500	9.6
2005-06	1,885,554,200	191,892,800	10.2
2006-07	1,953,623,000	231,010,300	11.8
2007-08	2,079,681,100	236,407,300	11.4
2008-09	2,038,723,100	270,124,900	13.2
2009-10	1,999,606,600	259,647,300	13.0
2010-11	1,991,313,500	253,730,000	12.7
2011-12	1,990,534,400	311,774,200	15.7
2012-13	2,021,915,600	316,782,500	15.7
2013-14	2,047,106,400	296,360,600	14.5
2014-15	2,040,521,700	281,871,800	13.8

¹⁾ Includes health care administration, clinical complexes, prisoner health care services, and vaccinations.

Source: Annual Year-to-Date Appropriations Acts

As the prisoner population has aged, the medical costs associated with taking care of the inmates have also risen by 79% in the past 16 years, as [Table 5](#) shows. There has been some moderating of the rising costs in the past couple of years, which may be an effect of the limited-risk capitation



health care model that the Department has had in place since 2009. As the demographics continue on a course of increasing age among the prisoner population, there should not be an expectation that health care costs will decrease.

Conclusion

As was the case the last time this subject was covered in a State Notes article (Spring 2010), there has been a decline in the prison population as well as in the number of FTEs but a lack of savings that might be expected. Since that time, the number of FTEs has decreased by nearly 2,000, but savings associated with these positions have not been realized due to two main factors: employee compensation including payment on unfunded accrued liabilities and increased prisoner health care costs mainly due to aging. Both factors are largely external to the annual appropriations process. The calculation of employee benefits is decided on a statewide basis and the provision of "non-deliberately indifferent" health care to prisoners has been required by courts.

As both the employees and the prisoners age, a greater amount of resources will be required to maintain the status quo of a stabilized prison population. As prison cohorts have moved through the system, the resources dedicated to provide for health care have gotten progressively greater. The population of elderly prisoners is likely to remain as large as in 2013, when 31% of the prison population was between the ages of 40 and 55. Employee benefits highlighted in Table 3 show that since FY 2002-03, the overall changes in employee economic costs have increased far more rapidly than the overall appropriation has, due to changes in calculating employee benefits and funding for unfunded accrued liabilities. To realize savings in the Corrections budget, any strategies undertaken must address the cost drivers of employee demographics and prisoner health care expenses.

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Where the Money Goes: Explaining the Price of Gasoline

By David Zin, Chief Economist

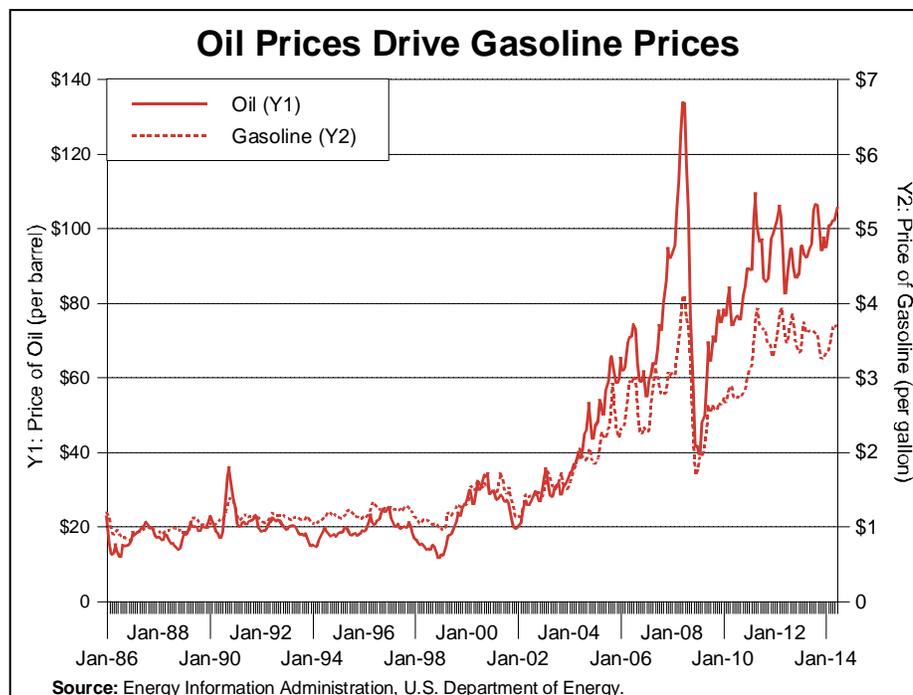
As the Legislature has debated a variety of options to generate additional revenue for repairing and maintaining Michigan's road and bridge system, much attention has been directed to the price of gasoline. This article discusses the recent history of gas prices; describes factors that comprise the price of a gallon of gasoline at the retail pump, as well as where Federal and State taxes are directed; and provides a few interstate and international comparisons on both prices and taxes.

A Brief History of Michigan Gas Prices

In February 1999, the average price of a gallon of regular gasoline in Michigan was 93 cents. A year later, the average price had risen to \$1.49 per gallon. In October 2004, the price of gas broke the \$2.00 per gallon barrier, at \$2.01, and rose to \$2.84 per gallon in September 2005. Prices jumped again in June 2007, averaging \$3.34 per gallon, and continued to rise, averaging \$4.11 per gallon in June 2008. Within six months, the price had fallen to \$1.68 per gallon but quickly bounced back to \$2.78 per gallon in June 2009. The price of gasoline began remaining consistently above the \$3.00 per gallon mark in December 2010, and on a monthly basis has yet to drop below that level. As of the end of July 2014, the average price of a gallon of gasoline in Michigan was \$3.46.

According to the Energy Information Administration, a division of the U.S. Department of Energy, changes in retail gasoline prices in the United States primarily reflect changes in crude oil prices (Figure 1). Crude oil prices are determined globally and economic growth in other countries has substantially increased the world's demand for oil since the early part of the century. Putting further pressure on oil prices, various supply disruptions have affected not only supply but the perceived risk to supply. These supply disruptions have included everything from natural disasters to political events in oil-producing countries to outages at U.S. refineries and pipelines.

Figure 1



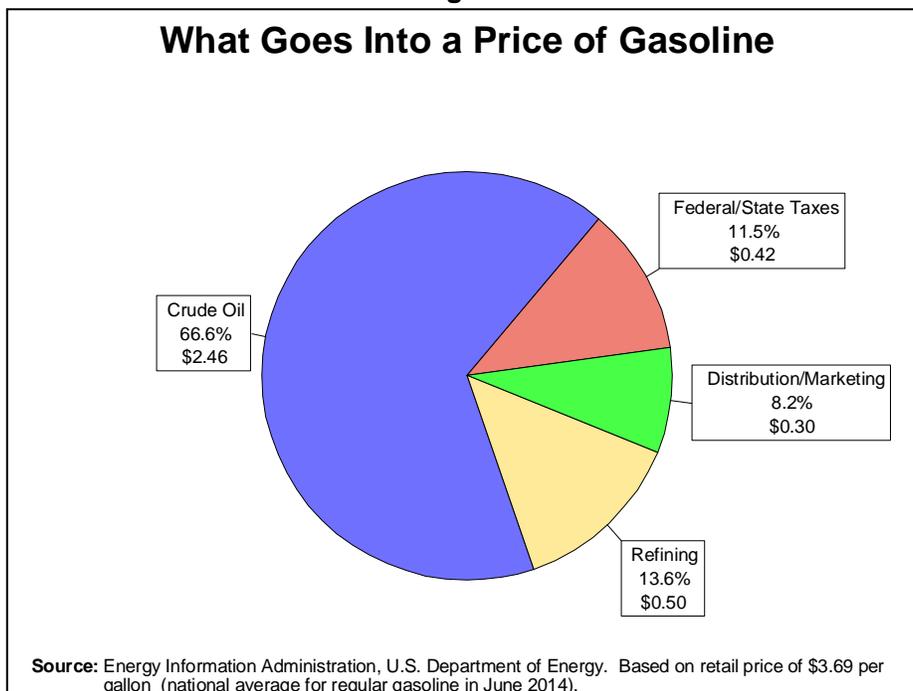
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The link between crude oil prices and retail gasoline prices exists because the majority (approximately 66.6%) of the price of gasoline at the pump reflects crude oil costs (Figure 2). Early in the 2000s, the price of crude oil accounted for approximately 35% to 40% of the price of a gallon of gasoline. As crude oil prices have risen more rapidly than other costs comprising the price of gasoline, the share attributable to crude oil has risen, occasionally reaching as much as 80.0% -- as happened in December 2011. Refining costs are the next-largest factor in gas prices, accounting for approximately 13.6% of the price, followed by Federal and state taxes (11.5%) and distribution and marketing costs (8.2%).

Figure 2



Federal and State Gasoline Taxes

The Federal tax on regular gasoline is 18.4 cents per gallon. The tax is per gallon and is not calculated based on the price of gas. As a result, the tax does not adjust for inflation and, as the price of oil rises, the tax becomes a smaller percentage of the price. State taxes include per-gallon taxes like the Federal gas tax and, in some states, sales taxes. Kentucky and North Carolina have tax rates that vary as the price of gasoline changes. Thirty-two states also have local motor fuel taxes or other environmental or administrative fees and taxes applied to gasoline in addition to the traditional fuel tax. Michigan is one of eight states that levies a sales tax on motor fuel in addition to a separate motor fuel tax, although the sales tax excludes the motor fuel tax from the tax base. Michigan's motor fuel tax is 19 cents per gallon for gasoline and 15 cents per gallon for diesel fuel. Like the Federal tax, Michigan's motor fuel taxes are not automatically adjusted for inflation and are independent of the underlying price of gasoline.

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The current Federal tax rate has been imposed since October 1993, while the current Michigan rate was last increased in 1997. Adjusted for inflation in the consumer price index, the 18.4 cents-per-gallon Federal tax would have been 29.8 cents per gallon in 2013, while the 19.0-cents-per-gallon Michigan tax would have been 26.7 cents. If the taxes had risen at the same rate as fuel prices (i.e., if the tax had remained the same percentage of the retail price), the Federal gasoline tax in June 2014 would have totaled 60.3 cents per gallon while the Michigan gasoline tax would have totaled 55.5 cents per gallon.

Since 1956, all of the revenue from the Federal gasoline tax has been directed to the Highway Trust Fund (HTF). The HTF was created in 1956 to ensure a dependable source of revenue for the National System of Interstate and Defense Highways. Before 1956, highway aid was funded by the U.S. Treasury's General Fund and motor fuel taxes were directed to that fund. With the expansion of Federal highway aid in the Federal-Aid Highway Act of 1956, the Highway Revenue Act began directing Federal motor fuel taxes to the HTF. Since 1956, programs funded by the HTF have expanded to include other transportation-related funding needs, such as other Federal-aid roads and mass transit programs.

Pursuant to provisions in Michigan's Constitution, revenue from both motor fuel taxes and vehicle registration fees must be used exclusively for transportation purposes. As a result, similar to the treatment of Federal motor fuel taxes, Michigan's motor fuel taxes are deposited in the Michigan Transportation Fund (MTF), although there is a constitutional earmark for 2% of the tax revenue from gasoline sales to the recreation improvement account in the Michigan Conservation and Recreation Legacy Fund to fund waterways, snowmobile trails, and other recreation projects. Revenue in the MTF is distributed according to Public Act 51 of 1951 and a portion of that revenue is directed to the State Trunkline Fund (STF), from which road construction and repair are funded. Motor fuel taxes deposited in the MTF totaled \$950.5 million in fiscal year (FY) 2012-13, and represented approximately 50.2% of total MTF revenue. Vehicle registration revenue accounted for \$906.5 million, or 47.9%, of FY 2012-13 MTF revenue.

Sales Taxes

As mentioned earlier, Michigan's sales tax is levied on motor fuel. Unlike the per-gallon motor fuel tax, the per-gallon amount of the sales tax changes as the price of motor fuel varies. When the price of gas averaged 93 cents per gallon in 1999, the motor fuel tax per gallon totaled 19 cents per gallon while the sales tax totaled about 4 cents per gallon. At the July 2014 price of \$3.46 per gallon for gasoline, the motor fuel tax remained at 19 cents but the sales tax also was approximately 19 cents per gallon.

Additionally, while the per-gallon motor fuel tax is directed to the MTF, sales taxes on gasoline are directed to a variety of other funds – almost all of which have no direct relation to transportation. Since the current State Constitution was adopted in 1963, 60% of sales tax revenue collected at a 4% tax rate has been directed to the School Aid Fund, and 15% of the collections at a 4% tax rate have been directed to constitutional revenue sharing to cities, villages, and townships. The passage of Proposal A's property tax and school finance reform in 1994 imposed an additional 2% on taxable sales and added constitutional provisions that direct to the School Aid Fund 100% of the revenue from the additional 2% sales tax. The Revenue Sharing Act statutorily earmarks 21.3% of the revenue collected at a 4% tax rate to statutory revenue sharing to cities, counties, townships, and villages, although the Legislature has not appropriated the full earmark since FY 2000-01. Another \$9.0 million is statutorily earmarked to health programs.

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The only provision that dedicates a portion of sales tax revenue to a transportation-related fund is a statutory earmark on 27.9% of the collections at a 1% tax rate from sales of transportation-related items to the Comprehensive Transportation Fund (CTF). In FY 2012-13, revenue from the sales tax earmark to the CTF totaled \$103.0 million. Most CTF revenue is directed to public transportation (mass transit) expenditures and is not directed to items such as road and bridge repair or construction.

Combined, the statutory and constitutional earmarks on sales tax revenue from sales of motor fuel mean that 83.3% of the sales tax is earmarked to the School Aid Fund and constitutional revenue sharing, and if revenue sharing were fully funded, a total of 102.2% of sales tax revenue from motor fuel would be earmarked in some way. Because the full earmark for revenue sharing is not funded, the revenue not appropriated to statutory revenue sharing is directed to the General Fund.

As a result, although Michigan gasoline prices are dominated by the price of crude oil, State taxes represent approximately 38 cents of the price of each gallon of gasoline, based on recent prices (Figure 3). Of those State taxes, 19 cents (the amount attributable to Michigan motor fuel taxes) are directed to the MTF. Of the remaining 19 cents of State taxes (from the sales tax), 14 cents are directed to the School Aid Fund, 2 cents are directed to constitutional revenue sharing, 2 cents are directed to the General Fund (of which a portion is appropriated to statutory revenue sharing), and the remaining 1 cent is directed to the CTF.

Figure 3

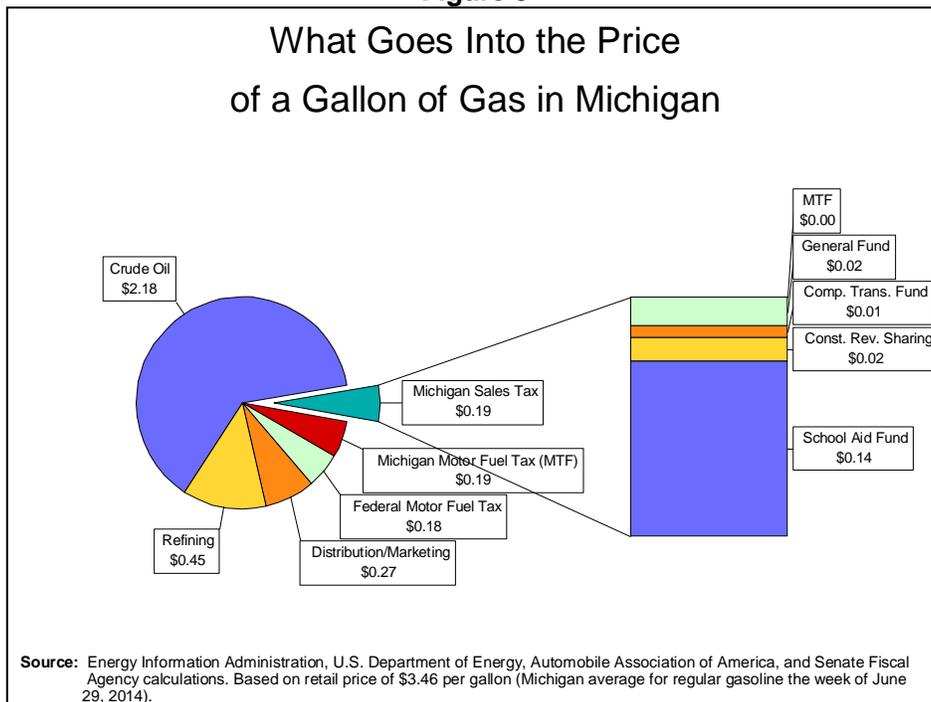


Table 1 presents a history of both motor fuel tax revenue and vehicle registration revenue to the MTF, as well as estimated sales tax revenue from sales of motor fuel and the portion of sales taxes on motor fuels that remains after constitutional earmarks. As fuel economy has risen and higher fuel prices have reduced some travel, revenue from motor fuel taxes was 7.0% less in FY 2012-13 than it was in FY 1997-98. If the figures were adjusted for inflation, the decline would be even greater. In

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contrast, despite some significant swings in revenue, higher vehicle prices have helped increase revenue from vehicle registrations by 36.3% over the same period. Sales tax revenue from motor fuel sales increased 267.0% over the period, driven entirely by the increase in the price of motor fuels.

Interstate and International Comparisons

As mentioned earlier, considerable variation exists between the tax rates different states levy on motor fuel. Although most states should, in theory, face roughly the same wholesale price for gasoline so that the differences in gasoline prices largely reflect transportation costs and state and local taxes, differences in wholesale prices do exist and can be significant. Table 2 shows that in June 2014, among the 46 states for which wholesale prices were available, the wholesale price in Oregon (the highest) was 12.4% above the price in North Carolina (the lowest). (Two of the states for which June data were not available, Alaska and Hawaii, exhibited the first- and second-highest wholesale prices in the annual data for 2013, and the gap between the highest and lowest wholesale prices was 21.4%.)

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Table 1
Revenue History for Select Michigan Transportation Taxes/Fees and Sales Taxes on Motor Fuel
(Dollar Amounts in Millions)

Fiscal Year	Gasoline Tax Revenue	Diesel Tax Revenue	Total Motor Fuel Tax Revenue	Percent Change	Vehicle Registration Taxes	Percent Change	Sales Tax on Gasoline	Sales Tax on Diesel	Total Sales Taxes on Motor Fuel	Percent Change	Sales Taxes on Fuel Not Const. Earmarked	Total Sales Tax Revenue	Sales Tax on Motor Fuel Share of Total Sales Tax
1997-98	\$904.5	\$118.4	\$1,022.9	---	\$665.3	---	\$236.3	\$40.9	\$277.2	---	\$46.2	\$5,617.3	4.9%
1998-99	931.7	134.7	1,066.4	4.3%	710.2	5.9%	270.0	44.9	315.0	13.6%	\$52.5	5,901.7	5.3%
1999-2000	923.0	144.1	1,067.1	0.1%	755.2	-1.1%	378.8	74.7	453.5	44.0%	\$75.6	6,277.5	7.2%
2001-01	934.4	133.7	1,068.1	0.1%	778.2	0.3%	364.1	66.5	430.6	-5.0%	\$71.8	6,352.3	6.8%
2001-202	939.7	143.4	1,083.1	1.4%	827.7	9.9%	334.5	63.4	398.0	-7.6%	\$66.3	6,441.2	6.2%
2002-03	936.2	157.3	1,093.5	1.0%	845.3	0.4%	388.5	80.4	468.9	17.8%	\$78.1	6,422.6	7.3%
2003-04	932.7	140.8	1,073.5	-1.8%	934.3	4.4%	464.4	87.5	551.9	17.7%	\$92.0	6,473.5	8.5%
2004-05	922.8	146.7	1,069.5	-0.4%	866.3	-17.3%	572.2	126.7	698.9	26.6%	\$116.5	6,599.1	10.6%
2005-06	906.7	149.0	1,055.7	-1.3%	870.4	-11.3%	638.8	145.6	784.5	12.2%	\$130.7	6,638.1	11.8%
2006-07	884.0	144.1	1,028.1	-2.6%	874.7	-3.7%	705.8	152.4	858.2	9.4%	\$143.0	6,552.2	13.1%
2007-08	849.2	140.4	989.6	-3.7%	857.9	-14.7%	780.6	194.3	974.9	13.6%	\$162.5	6,773.3	14.4%
2008-09	846.3	117.9	964.3	-2.6%	842.4	4.4%	546.8	101.9	648.8	-33.5%	\$108.1	6,089.1	10.7%
2009-10	842.0	120.3	962.3	-0.2%	844.9	-3.3%	655.0	127.8	782.8	20.7%	\$130.5	6,176.1	12.7%
2010-11	832.0	125.9	957.9	-0.5%	862.5	-5.7%	839.5	178.1	1,017.6	30.0%	\$169.6	6,709.0	15.2%
2011-12	818.8	126.8	945.6	-1.3%	876.1	-1.5%	853.5	184.2	1,037.7	2.0%	\$172.9	6,952.8	14.9%
2012-13	822.0	129.2	951.1	0.6%	906.5	2.7%	830.6	186.7	1,017.3	-2.0%	\$169.5	7,153.8	14.2%

Source: Comprehensive Annual Financial Report, Michigan Department of Technology, Management, and Budget; Automobile Association of America; Senate Fiscal Agency calculations

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Table 2

State Gasoline Taxes, 2014									
State	Tax Rate (cents/gallon)	Rank	State Sales Tax (effective cents/gallon)	Combined Rates (cents/gallon)	Rank	Wholesale Price of Gas June 2014	Rank	Retail Price of Gas 07/29/2014	Rank
Alabama	18.000	41		18.000	44	2.874	45	\$3.269	48
Alaska	8.000	50		8.000	50		N/A	4.145	2
Arizona	19.000	37		19.000	41	3.053	13	3.535	24
Arkansas	21.800	30		21.800	36	2.924	37	3.318	44
California	46.500	1	7.759	54.259	1	3.138	3	3.991	3
Colorado	22.000	28		22.000	34	3.002	21	3.612	18
Connecticut	25.000	20		25.000	26	3.080	9	3.893	6
Delaware	23.000	26		23.000	32	3.027	17	3.446	30
Florida	17.100	44	18.538	35.638	9	2.923	38	3.446	30
Georgia	19.300	36	12.427	31.727	14	2.935	36	3.424	34
Hawaii	17.000	45	16.027	33.027	10		N/A	4.337	1
Idaho	26.000	18		26.000	24	3.068	10	3.778	9
Illinois	20.100	33	19.659	39.759	4	3.085	8	3.543	23
Indiana	18.000	41	20.961	38.961	5	3.007	20	3.384	37
Iowa	22.000	28		22.000	34	2.954	32	3.394	36
Kansas	25.030	19		25.030	25	2.908	40	3.332	43
Kentucky	30.800	9		30.800	15	3.117	4	3.407	35
Louisiana	20.125	32		20.125	38	2.899	41	3.356	40
Maine	30.000	10		30.000	16	3.035	15	3.650	13
Maryland	27.000	15		27.000	21	3.023	18	3.550	21
Massachusetts	24.000	22		24.000	28	3.055	12	3.642	15
Michigan	19.000	37	18.487	37.487	8	3.088	6	3.456	28
Minnesota	28.600	12		28.600	18	2.888	42	3.376	39
Mississippi	18.400	40		18.400	43	2.886	43	3.310	45
Missouri	17.300	43		17.300	45	2.944	33	3.258	49
Montana	27.000	15		27.000	21	2.965	29	3.619	17
Nebraska	27.300	14		27.300	20	2.958	31	3.431	33
Nevada	23.805	25		23.805	31	3.104	5	3.811	8
New Hampshire	19.625	35		19.625	40		N/A	3.595	20
New Jersey	14.500	48		14.500	48	2.996	22	3.441	32

State Notes
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Table 2 (continued)

State Gasoline Taxes, 2014									
State	Tax Rate (cents/gallon)	Rank	State Sales Tax (effective cents/gallon)	Combined Rates (cents/gallon)	Rank	Wholesale Price of Gas June 2014	Rank	Retail Price of Gas 07/29/2014	Rank
New Mexico	18.875	39		18.875	42	2.980	26	3.491	27
New York	26.400	17		26.400	23	3.031	16	3.847	7
North Carolina	37.750	3		37.750	6	2.862	46	3.451	29
North Dakota	23.000	26		23.000	32	2.992	23	3.548	22
Ohio	28.000	13		28.000	19	3.067	11	3.354	41
Oklahoma	17.000	45		17.000	46	2.967	27	3.302	46
Oregon	30.000	10		30.000	16	3.217	1	3.927	4
Pennsylvania	40.700	2		40.700	3	2.966	28	3.643	14
Rhode Island	33.000	6		33.000	11	3.087	7	3.665	12
South Carolina	16.750	47		16.750	47	2.876	44	3.257	50
South Dakota	24.000	22		24.000	28	2.961	30	3.497	26
Tennessee	21.400	31		21.400	37	2.911	39	3.298	47
Texas	20.000	34		20.000	39	2.938	34	3.384	37
Utah	24.500	21		24.500	27	3.047	14	3.703	10
Vermont	31.970	8		31.970	13		N/A	3.693	11
Virginia	11.100	49		11.100	49	2.983	25	3.333	42
Washington	37.500	4		37.500	7	3.156	2	3.925	5
West Virginia	35.700	5	18.413	54.113	2	2.990	24	3.610	19
Wisconsin	32.900	7		32.900	12	3.016	19	3.511	25
Wyoming	24.000	22		24.000	28	2.938	34	3.624	16
Federal Tax	18.400			18.400					
U.S. Average						2.812		3.515	

Sources: Federation of Tax Administrators, Automobile Association of America, Senate Fiscal Agency calculations

State Notes

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Generally, tax rates are highest in the New England, Middle Atlantic, and Western states; and lowest in the Central, Southern, and Southeastern states. Similarly, average retail prices tend to be higher in the regions with higher tax rates, and lower in the regions with lower tax rates. However, numerous exceptions weaken that correlation. For example, Michigan's motor fuel tax rate ranks 37th out of the 50 states; but if sales taxes levied on motor fuels are included, the ranking rises to eighth, although it should be noted that the ranking overstates Michigan's position particularly because Michigan does not levy any local taxes on gasoline. For example, in Nevada (which ranks 31st) local sales taxes range from four to nine cents per gallon, and those taxes would raise Nevada's ranking to somewhere between 20th and 13th depending on the local unit. Similarly, in Florida, local taxes can range from 10.8 cents to 19.1 cents per gallon, and there is a 2.071-cent-per-gallon pollution tax not included in price rankings. Motor carriers are assessed additional taxes in some states such as in Illinois, where carriers pay an additional 19.5 cents per gallon. Although Michigan ranked eighth for total state taxes on motor fuel, and sixth for wholesale price in June 2014, Michigan's average retail price ranked 28th the week of June 29, 2014, and over the last 14 years, Michigan's retail prices have ranked between 22nd and 37th. Among surrounding states, Michigan's average retail prices fall in the middle. Prices in Illinois and Wisconsin are usually above Michigan's price, while those in Indiana and Ohio generally fall below Michigan's.

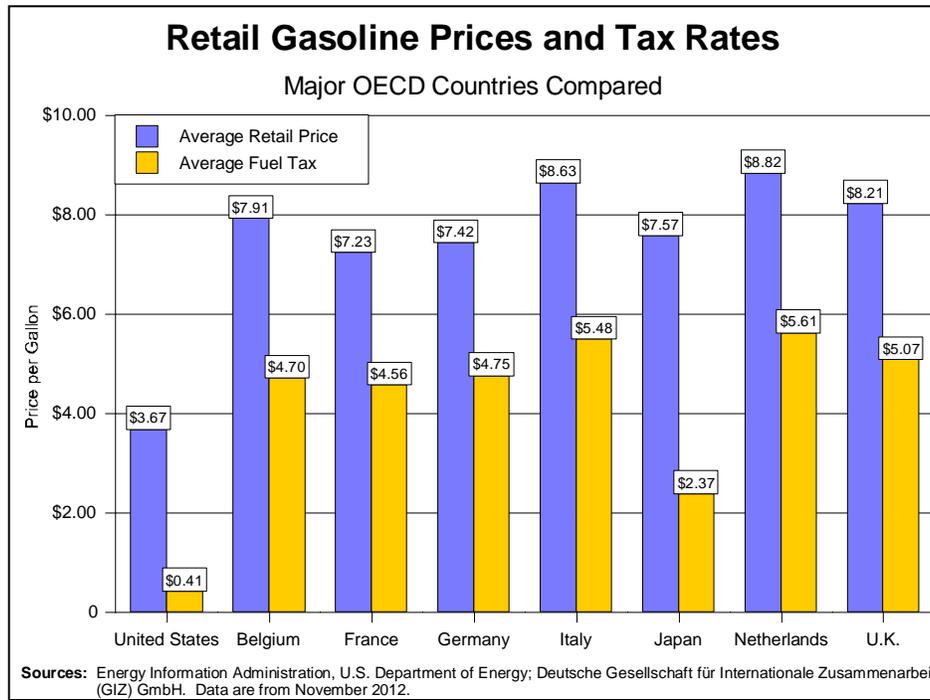
Compared with other countries, the United States exhibits both lower levels of taxation and lower retail prices. Approximately 19 countries, mostly members of the Organization of Petroleum Exporting Countries (OPEC), heavily subsidize retail gasoline prices. Venezuela offers the most significant subsidies, so its average retail price of gasoline is approximately 8.7 cents per gallon. Libya exhibits the next-lowest retail prices, at 45.4 cents per gallon. Among countries with the most significant retail subsidies, the highest gas price is in Angola, at \$2.38 per gallon.

Another 10 countries, mostly a few Central American and northern African countries, slightly subsidize gasoline prices, with prices varying from \$2.65 per gallon to \$3.67 per gallon. The retail price of gasoline in the United States is generally regarded as reflecting a cost-covering price, where costs include industry margins, necessary taxes to support road funding, etc., although external health and environmental costs are not covered. In November 2012, the period from which these comparisons are reported, the average retail price of gasoline in the U.S. was \$3.67 per gallon.

The majority of countries tax gasoline more heavily than the United States does. In countries that are not considered high fuel tax countries, average retail prices range from \$3.75 per gallon in Russia to \$6.17 per gallon in Peru. These "moderate taxation" countries represent the majority of countries and span the globe, although Western Hemisphere countries tend to be more prevalent on the low end of the range while African and Asian countries are more common on the high end.

Finally, approximately 60 countries (almost as many as in the "moderate taxation" group) are considered "high taxation" countries. These countries are effectively using fuel taxes to generate revenue and to encourage energy efficiency in the transportation sector, and the average retail prices range from \$6.21 per gallon in Luxembourg to \$9.61 per gallon in Turkey and Norway. The majority of "high taxation" countries are located in Europe. Compared with prices in major Organization for Economic Cooperation and Development (OECD) countries, using the exchange rates effective in November 2012, the average retail price of gasoline in the United States is approximately half of that in other major OECD countries, and the combined Federal and state tax rates are approximately one-tenth of the rate in those countries ([Figure 4](#)).

Figure 4



Conclusion

In the United States, the price of crude oil accounts for both the majority of the price of gasoline and changes in the price of gasoline over time. Both Federal and state taxes on motor fuels provide funding for the road system and both tax rates and retail prices vary significantly across states. Michigan's motor fuel tax rate is below the rate in most states, although this is somewhat offset by sales taxes levied on motor fuel sales. However, in many other states, local motor fuel taxes also are levied or other fees and taxes are imposed on the sale of motor fuels. Inclusive of all taxes and fees, Michigan retail gasoline prices tend to be slightly below the national average and in the middle of those in other Great Lakes states. Both retail prices for gasoline and motor fuel tax rates are lower in the United States than in most developed countries.

The revenue generated by Michigan's motor fuel taxes has declined as vehicles have become more fuel efficient and the rising price of gasoline has encouraged greater efforts at conservation. Sales taxes levied on motor fuel sales are largely earmarked by constitutional provisions that direct almost three-fourths of the revenue to education and 10% to local units of government. The buying power of the revenue generated by Michigan's motor fuel taxes has been substantially eroded by inflation. Adjusting Michigan's motor fuel tax rates to reflect inflation would substantially increase the tax rate. As long as the tax rate remains fixed and is not subject to automatic adjustments, the buying power of the revenue generated will decline in future years.

Regardless of how the State resolves the debate on road and bridge funding, the primary influence on the price of gasoline is likely to remain the price of crude oil. Similarly, revenue will continue to be affected by inflation and the changing demographics of motor fuel consumption.

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A Summary of Patent Troll Activity and State Law By Jeffrey Mann, Legislative Analyst

Introduction

Patents are generally perceived to be a net social good, exchanging a limited-time right to exclude others from making an invention for the public disclosure of that knowledge. Recently, however, the proliferation of many computer and business method patents and associated litigation conducted by entities that do not practice these patents have led some to recommend legislative changes meant to ensure that assertions of patent infringement are made in good faith.¹ In Michigan, a bill that was recently introduced in the House of Representatives is purported to do exactly that. This article begins by introducing the basic concepts of patents and the Federal law of patents. A brief overview of nonpracticing entities follows. The article then discusses issues and arguments pertaining to the perceived merits and shortcomings of patent assertion entities. Finally, the article introduces the concept of state regulation as an approach to restricting bad-faith demand letters², and briefly discusses the bill introduced in the Michigan House of Representatives.

Basics of Patents and Patent Laws

A patent is a right granted by a government to an inventor to exclude others from making, using, or selling an invention for a defined period of time.³ Patents function as a *quid pro quo* of sorts in that the rights granted by a patent are a limited-time monopoly in exchange for a disclosure of the invention to the public. This, in theory, creates an incentive for inventors and entrepreneurs to allocate money and resources to developing new technology in the hopes that they will be able to patent the invention and derive the benefits from the patent, while disclosing to society the way the invention works. In the United States, the patent system is specifically provided for in the U.S. Constitution, and is regulated under Federal law.⁴ Patents are granted by the United States Patent and Trademark Office (USPTO), which resides within the Department of Commerce.

To qualify for a patent, an invention must meet four basic requirements. First, the invention must be patentable subject matter. Patentable subject matter includes any process, machine, manufacture, or composition of matter; laws of nature, abstract ideas, or natural phenomena are not patentable.⁵ Second, an invention must be useful.⁶ The third requirement is that the invention be novel. An invention is not considered novel if the invention "was patented, described in a printed publication, or in public use, on sale, or otherwise available to the public before the effective filing date of the

¹ An entity that "practices" its patents uses them to design or manufacture products or processes.

² As discussed below, such letters demand that an alleged patent infringer buy a license in order to avoid being sued.

³ It is a common misconception that a patent grants a patentee the right to practice the invention. A patent cannot grant such a right because one patent might be dependent on another patent to practice a particular technology. A patent granted from an application filed after June 8, 1995, is valid for 20 years from the filing date of the application. Before June 8, 1995, a patent was valid for 17 years from its issue date. The term can be adjusted because of examining delays or, for pharmaceutical patents, delays associated with gaining U.S. Food and Drug Administration approval.

⁴ Specifically, Congress has the power to "promote the progress of science and useful arts, by securing for limited times to...inventors the exclusive right to their...discoveries", U.S. Constitution Art. I, § 8, cl.8.

⁵ 35 U.S.C. § 101.

⁶ *Id.* As a general matter, patents are seldom challenged on utility grounds.



claimed invention", unless certain conditions are met.⁷ Finally, the invention must be nonobvious. An invention is nonobvious when, at the time the invention was made, it would not have been obvious to a person having ordinary skill in the art pertaining to the invention.⁸

To obtain a patent, one must file a patent application with the USPTO. The first inventor to file an application is awarded the patent.⁹ The application must disclose the best mode for practicing the invention, and must meet the "enablement" requirement; that is, the application must disclose the invention in a manner that allows a person skilled in the art to make and use the invention without undue experimentation.¹⁰ The application is reviewed by an examiner who analyzes the patent for compliance with all the applicable patent laws and regulations and either grants, or more typically, rejects the patent application. The application may go through multiple rounds of amendment and rejection before the application is granted, and a patent is issued, or the application is abandoned. A patent is composed of two general parts: 1) a specification, which describes a technical background of the problem the patent attempts to solve, a description of the invention, a drawing of the invention, and other information pertaining to the claimed invention, and 2) a set of claims, which articulate exactly what is covered under the patent.

Patents are considered personal property and are treated accordingly. While only an inventor can file for a patent, any legal person can own patents.¹¹ Patents can be licensed, assigned, abandoned, donated to the public, or used as security.¹² Patent rights are enforced primarily through an infringement suit, or the threat of such a suit. A person who, without authority, imports, makes, uses, or sells a product covered by a patent is liable as an infringer.¹³ This is considered direct infringement. A person also can indirectly infringe by actively inducing another to infringe,¹⁴ or by selling, offering to sell, or importing a component of a material part of a patented invention knowing the component was made or adapted for use in an infringement.¹⁵ Damages against an infringer can

⁷ 35 U.S.C. § 102. The conditions have to do with certain activities of the inventor that are beyond the scope of this paper.

⁸ 35 U.S.C. § 103. This is often called the PHOSITA (person having ordinary skill in the art) test. The PHOSITA is a "legal fiction", much like the reasonably prudent person in United States tort law.

⁹ Until the America Invents Act was passed, the United States was one of a few countries that had a "first to invent" requirement.

¹⁰ The best mode requirement requires the inventor, in the specification of the patent, to set forth the best way to practice the invention. 35 U.S.C. § 112(a). Enablement also is required under § 112(a); the undue experimentation test was set forth by the U.S. Supreme Court in *Mineral Separation v. Hyde*, 242 U.S. 261, 270 (1916).

¹¹ An inventor must be a natural person. Many of the patents that are applied for are done so on behalf of large companies involved in high-technology research and development. It is a customary condition of employment at these companies that any patent granted to an employee of the company for an invention developed in the course of his or her employment or that used company resources must be assigned to the company.

¹² The licensing of patents takes two forms: exclusive and nonexclusive. An exclusive license grants all rights under the patent to the licensee, and the patent owner retains title to the patent. An exclusive license can be limited to field or geography. This means that multiple exclusive licenses can be granted. If the field or the geographical scope of the license is limited, the licensee can exercise all of the rights within the scope of field or geography. A nonexclusive license is basically a forbearance from an infringement lawsuit granted to a licensee.

¹³ 35 U.S.C. § 271(a).

¹⁴ 35 U.S.C. § 271(b).

¹⁵ 35 U.S.C. § 271(c).



be extensive. At a minimum, the infringer is subject to damages that equal a reasonable royalty, but also may include lost profits, and for certain cases, treble damages, attorney fees, and costs.¹⁶

Nonpracticing Entities and Patent Assertion Entities

A nonpracticing entity (NPE) holds a patent for a process or product but does not exercise the underlying art. There are many reasons why an entity may choose not to practice a patented technology. For example, most universities are considered NPEs. A university's faculty members, particularly those in high-technology sectors such as biotechnology or engineering disciplines, might develop patentable technologies in the course of their research. The university might have the resources to secure a patent, but not to bring the product to market. University technology transfer offices will license the patents, usually exclusively, to companies that are capable of developing the technology.¹⁷ Large companies also qualify as NPEs to the extent that they purchase patents through subsidiaries to assert against their competition or to use them defensively.¹⁸

Another group of NPEs are the so-called "patent assertion entities" (PAEs). These companies operate by purchasing patents and holding them in a portfolio. The patents might come from a variety of sources, such as a failed business looking to liquidate its patent portfolio or a small-scale inventor who cannot afford to develop the technology on his or her own. A PAE will not practice the art and generally will not grant a license preemptively. Instead, the PAE will monitor the market for products or processes that could infringe on a patent in its portfolio. In some cases, PAEs have been accused of waiting until a company makes a significant investment or takes other irreversible action on technology that the PAEs believe is covered by the patent.¹⁹ When infringement activity is suspected, the entity will issue a demand letter requesting that the suspected infringer take a nonexclusive license to avoid being sued. Occasionally, these letters are sent indiscriminately and there have been reported instances in which a form demand letter was sent to multiple parties.²⁰ Sometimes, a demand letter expresses nothing more than a vague statement or assertion that the party to whom the letter is addressed might be infringing an unnamed patent, or patents. Because of these tactics, PAE detractors have used colorful pejorative nicknames such as "patent sharks", "patent pirates", and more commonly, "patent trolls".²¹

¹⁶ 35 U.S.C. §§ 283-285. Treble damages are typically awarded in instances of willful infringement.

¹⁷ See Mark A. Lemley, "Are Universities Patent Trolls?", 18 *Fordham Intellectual Property, Media and Entertainment Law Journal* 611 (2008) for an in-depth discussion of university patent licensing and technology transfer activities and the resulting issues.

¹⁸ A patent litigation strategy employed by large industrial entities has been to purchase a large number of patents related to the technology they research, manufacture, and sell. These patents may be used to develop new technology or conduct research, but they can also be asserted in a counterclaim against a party who has claimed infringement. This kind of "mutually assured destruction" can sometimes keep litigation from going too far.

¹⁹ See "Patent Assertion and U.S. Innovation", Executive Office of the President, p. 4 (2013).

²⁰ In one case, a PAE sent nearly 8,000 demand letters to various suspected infringers. See Ashby Jones, "Cisco's Patent Counterattack Fails", *Wall Street Journal*, 2-6-2013, retrieved 10-13-2014 at: <http://online.wsj.com/news/articles/SB10001424127887324906004578288370005621206>.

²¹ The term "patent troll" was coined by the Intel legal team from the mythical beast who hides under a bridge it did not build to demand a toll from people crossing the bridge.



The Growth of Trolls

Some believe that the business tactics described above are the consequence of a combination of issues endemic within the patent legal landscape and the technological backdrop of the last 20 years. Several studies have demonstrated a marked increase in PAE litigation activity. In 2010, PAEs brought approximately 731 lawsuits, or 29% of all patent lawsuits.²² In 2012, the number was 2,500 lawsuits, nearly 62% of all patents lawsuits. There are a few likely reasons for this increase.

The first factor has to do with the patent litigation landscape and how PAEs fit into it. In most nations, the rule for assigning costs for conducting litigation is the so-called "loser pays" system in which the party that loses the case pays its costs and the winner's litigation costs.²³ In the United States, this is generally not the case; each party pays its own costs. Filing a lawsuit in the United States is also relatively inexpensive. For these reasons, the barrier to entering into a patent lawsuit can be fairly low.

On the other hand, patent litigation between traditional parties can entail a high amount of risk. First, litigating a patent can be quite expensive.²⁴ These trials require specific experts, specially trained attorneys, and extensive discovery. The process can be significantly more expensive if a large company decides to employ a protracted, "scorched earth" litigation strategy as a tactic (usually against a smaller or less well funded competitor).²⁵ Second, an accused infringer will usually stop researching and marketing an infringing product. This costs time and money; however, if it continues to infringe, the infringer could be subject to treble damages, in addition to lost profits, attorney fees, costs, and the prospect of having to negotiate a license with a party whose patent was willfully infringed. Moreover, the traditional plaintiff also must tread lightly, as the defendant could counterclaim for infringement of its own patents, the plaintiff could be seen as a bully from a public relations perspective, or a court could easily invalidate the infringed patent, ending a stream of licensing royalties. These factors have encouraged a scheme of settlement, negotiation, licensing, and cross-licensing.²⁶

²² Colleen Chien, "Patent Assertion Entities" Presentation at Joint Federal Trade Commission and Department of Justice Workshop on PAEs, 12-10-2012:
<http://www.justice.gov/atr/public/workshops/pae/>. It is not clear if the numbers cited in this presentation take into account changes to joinder of parties set forth by the America Invents Act, which would have likely increased the total number of cases filed, but not the total amount of actual activity. For a discussion of these changes, see Maya M. Eckstein, et al., "The (Unintended) Consequences of the AIA Joinder Provision", Paper, AIPLA Spring Meeting, 5-2012:
<http://www.hunton.com/professionals/uniEntity.aspx?xpST=ProfessionalDetail&professional=145&op=publications&ajax=no>.

²³ Marie Gryphon, "Greater Justice, Lower Cost: How a 'Loser Pays' Rule Would Improve the American Legal System", *Civil Justice Report* No. 11-Manhattan Institute for Policy Research (2008):
http://www.manhattan-institute.org/html/cjr_11.htm.

²⁴ The American Intellectual Property Law Association (AIPLA) conducted a survey of its members in 2011. The survey indicated that the median cost of litigating a patent can range from \$650,000 (where less than \$1 million is at risk) to \$5 million (more than \$25 million at risk). See American Intellectual Property Law Association, "Re: Comments on the FTC/DOJ Patent Assertion Entity Activities Workshop, December 10, 2012." 4-5-2013
<http://www.justice.gov/atr/public/workshops/pae/comments/paew-0046.pdf>.

²⁵ M. Craig Tyler, "Patent Pirates Search for Texas Treasure", *Texas Lawyer*, 9-20-2004.

²⁶ See n. 17, at 5.



By virtue of their business model, PAEs eliminate most of these risks, while taking advantage of the low barrier to file lawsuits. First, demand letters, especially those with vague assertions of patent infringement, are inexpensive and can be widely disseminated, scaring some businesses into taking a license immediately. Many PAEs have attorneys who charge on a contingency basis, which keeps the PAEs' initial costs of filing lawsuits and other preliminary work low.²⁷ The documents needed for discovery and trial are typically produced ahead of time. As a rule, PAEs have few employees and few assets (with the exception of their patent portfolio).²⁸ A PAE generally does not need to worry about public perceptions because it does not market products to the public. Meanwhile, because a PAE does not have product lines, does not conduct research and development, and will not lose money from not putting out a potentially infringing product, the time and cost of defending a patent lawsuit work to the PAE's advantage. For these reasons, PAEs also are less vulnerable to "scorched earth" litigation employed by large companies.

Another set of issues pertains to the type of technology involved in the patents being asserted by PAEs. A wide range of technology is subject to the patent preparation and prosecution process.²⁹ Some fields, such as biotechnology and pharmaceuticals, rely heavily on the 20-year term of patents to recoup the significant investments needed to bring products to market. It has been argued that other inventions, typically those involving communications, software, and computers, are rendered obsolete more quickly, have wider claim breadth, and are accordingly subject to greater abuse.³⁰

Supporters of PAEs argue that these entities generate a secondary market for patents, particularly for individuals or businesses that might need to sell patents quickly for any number of reasons, or that prosecute a patent but do not wish to maintain it in their portfolio.³¹ There is some evidence suggesting that this secondary market is helpful and drives innovation to some degree by providing small-scale inventors and start-ups with needed capital.³² In addition, some claim that PAEs reduce transaction costs and give small-scale inventors a chance to enforce their patent rights at the expense of large companies that might engage in protracted litigation.³³

On the other hand, detractors contend that PAE activities run contrary to the intent of the patent system and are a net drag on the economy.³⁴ Reportedly, the vast majority of money extracted from settlements and lawsuits has not gone to individuals or start-ups, but rather to the companies conducting these activities.³⁵ In addition, some contend that PAEs assert improperly granted, and

²⁷ Tyler, n. 23.

²⁸ *Id.*

²⁹ The term "prosecution" typically relates to plaintiff-side litigation; however, in patent parlance, prosecution relates to a patent attorney and inventor's interactions with patent examiners throughout the patent application process and subsequent interactions with the USPTO once the patent is granted.

³⁰ See n. 17, at 7-9; Thomas A. Hemphill, "The Paradox of Patent Assertion Entities", *The American Magazine*, 8-12-2013, retrieved 10-13-14 at: <http://www.american.com/archive/2013/august/the-paradox-of-patent-assertion-entities>, for a discussion on this point.

³¹ See Hemphill, n. 28.

³² See Chien, n. 20.

³³ See Hemphill, n. 28.

³⁴ See n.17, at 12; Hemphill, n. 28.

³⁵ James E. Bessen, et al., "The Private and Social Costs of Patent Trolls", Boston University School of Law, Law and Economics Research Paper No. 11-45, 9-19-2011.



often weak, patents.³⁶ In doing so, they derive income from asymmetrical "warfare". This, detractors claim, ultimately creates barriers to entry for entrepreneurs and small businesses, and hampers innovation.³⁷

Regulation of NPEs and Infringement Suits

While there is definite interest in curbing certain practices of PAEs at the Federal level, most efforts designed to achieve that end have stalled.³⁸ Since early 2013, states have attempted to alleviate the perceived problems of PAEs through the legal mechanisms available to them. Most of these efforts focus on a PAE's practice of issuing vague or misleading demand letters. In May 2013, Vermont enacted the first state law regulating patent trolls.³⁹ Since then, according to the National Conference of State Legislatures, at least 17 other states have passed similar measures, and other states, including Michigan, have proposed such legislation.⁴⁰

Some of these efforts, including Michigan's House Bill 5701, attempt to differentiate between a "good faith demand letter" and a "bad faith demand letter". One of the preferred mechanisms for doing this in the legislation is to amend the state's unfair or deceptive trade practices law, while other laws or bills create or propose a new act governing the practice of issuing demand letters.⁴¹

House Bill 5701, sponsored by Representative Mike Callton and referred to the House Committee on Michigan Competitiveness, would enact the "Bad-Faith Patent Infringement Claims Act". The bill would prohibit a person from making a bad faith assertion of patent infringement, and would allow a court to consider certain factors as evidence of a bad faith assertion. Factors to be considered would include, for example, not providing certain information in a demand letter (for instance, the patent number or patentee or assignee information), demanding unreasonable royalty fees, or failing to conduct an analysis comparing the patent's claims to the target's products, services, or technology. The bill also would prescribe factors for determining what would constitute a good faith assertion of patent infringement. Like many of the other states' legislation, House Bill 5701 would allow the Attorney General to conduct civil investigations and bring civil actions. The bill also would allow the target of a bad faith assertion to bring a civil action. If successful, the target could receive equitable

³⁶ This assertion is commonly made, with mixed support from scholars and attorneys. See, for example, Hunter Keeton & Edmund J. Walsh, "Death Knell for Patent Trolls", *Asia IP*, 5-2012: <http://www.wolfgreenfield.com/newsstand/522-death-knell-patent-trolls>; compare with Timo Fischer & Joachim Henkel, "Patent trolls on markets for technology – An empirical analysis of NPEs' patent acquisitions", 41 *Research Policy* 1519, 11-2012 (arguing that patents held by NPEs are of higher quality than those held by practicing entities).

³⁷ See n. 17 & 33.

³⁸ See, for example, Kate Tummarello, "Patent reform bill dealt fatal blow in Senate", *The Hill*, 5-21-2014, retrieved 10-15-2014, at: <http://thehill.com/policy/technology/206793-leahy-takes-patent-reform-off-committee-agenda>.

³⁹ Eric Goldman, "Vermont Enacts The Nation's First Anti-Patent Trolling Law", *Forbes*, 5-22-2013, retrieved 10-15-2014, at: <http://www.forbes.com/sites/ericgoldman/2013/05/22/vermont-enacts-the-nations-first-anti-patent-trolling-law/>.

⁴⁰ "Patent Trolling Legislation", National Conference of State Legislatures, 10-13-14: <http://www.ncsl.org/research/financial-services-and-commerce/patent-trolling-legislation.aspx>.

⁴¹ Compare, for example, Louisiana's House Bill 564 (2014), at <http://www.legis.la.gov/legis/BillInfo.aspx?s=14RS&b=HB564&sbi=y>, with Michigan's H.B. 5701 (2014), available at the Michigan Legislature website: <http://www.legislature.mi.gov>.



remedies, damages, costs and attorney fees, and exemplary damages equal to \$50,000 or treble damages, whichever were greater.

State efforts to regulate PAE conduct will likely be reviewed by the courts in the near future. The main issue that will confront such legislation is whether it would be preempted by the Federal law governing patents. The United States Constitution establishes the Constitution, Federal statutes, and treaties as the "supreme law of the land".⁴² From this, the courts have fashioned the doctrine of Federal preemption. There are three types of Federal preemption: express preemption, conflict preemption, and field preemption. Express preemption occurs when a Federal statute explicitly indicates Congress's intent that the statute supersede state laws.⁴³ Under conflict preemption, state law is preempted if it conflicts with Federal law. A conflict occurs if the state law is an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.⁴⁴ A conflict also occurs if a party is unable to comply with Federal and state law.⁴⁵ In the absence of a conflict or an express intent to supersede state law, a court may still infer intent to preempt state law if the Federal regulatory scheme is so pervasive as to "occupy the field" in that area of the law.⁴⁶ For some of the measures being advanced, a conflict could arise if a factor considered evidence of a bad faith demand letter is an activity permitted by the law of patents.

Conclusion

Notwithstanding concerns of Federal preemption, a state law prohibiting an entity from making a bad faith assertion of patent infringement with well-defined "bad faith" factors could be an effective way to prevent abusive patent litigation while ensuring that those whose patents are actually being infringed have an avenue to address their concerns with the infringer. It also could ensure that those who are innovating, producing, and marketing in good faith have sufficient information to continue their operations and could enable them to make well-informed licensing decisions if the need arises. A cautious approach with regard to PAEs may separate those entities who are interested in acting as a beneficial intermediary for small-scale investors in their assertion of patents from those who are not.

⁴² Specifically, Article VI, cl. 2 states, "This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, any thing in the Constitution or laws of any state to the contrary notwithstanding."

⁴³ *English v. General Electric*, 496 U.S. 72, 78-79 (1990).

⁴⁴ *Gade v. National Solid Wastes Management Association*, 505 U.S. 88, 115 (1992).

⁴⁵ *Id.*

⁴⁶ *Id.* at 98.

State Notes

TOPICS OF LEGISLATIVE INTEREST

Fall 2014



The "Heat and Eat" Policy in Michigan **By Frances Carley, Fiscal Analyst**

Summary

The State of Michigan recently ended its participation in what is known as the "Heat and Eat" policy. As a result, approximately 18.2% of the Food Assistance Program (FAP) cases will see an average decrease in their monthly food benefits of \$76.73.¹ While many states are choosing to continue the policy under new Federal guidelines that increased the program costs, that approach in Michigan could result in a reduction in the amount of Federal funding that is available for low-income heating and energy assistance.

Background on Michigan's Heat and Eat Policy

During the economic downturn in 2010, Michigan began participating in the Heat and Eat policy, also known as \$1 Low-Income Home Energy Assistance Program (LIHEAP). When changes to Federal funding requirements took effect in Michigan on May 1, 2014, the Department of Human Services (DHS) began to phase the policy out.

The State had used the Heat and Eat policy to maximize food assistance payments. Statewide, it increased the amount of Federal food assistance that was available to Michiganders by approximately \$146.4 million annually. The policy allowed the DHS to provide \$1 in LIHEAP funding to households receiving FAP benefits so that they could claim additional Federal funding for food assistance each month. From 2010 to 2014, the State spending plans had allocated up to \$1.0 million of Federal LIHEAP funding for Heat and Eat. Actual spending per year was between \$400,000 and \$475,000.

Under current Federal law, however, the DHS would have to provide more than \$20 in LIHEAP funding to households receiving FAP benefits in order for them to obtain additional food assistance (as explained in detail below). The Heat and Eat policy is being phased out, as the effective dates will vary by case and will depend on the FAP redetermination date for each case. Many FAP recipients who do not qualify for the expanded benefits have begun to be affected by the reductions.

Federal Funding for the Heat and Eat Policy

The Heat and Eat policy used two sources of Federal funding: the Low-Income Home Energy Assistance Program and the Supplemental Nutrition Assistance Program.

Low-Income Home Energy Assistance Program: The State receives Federal block grant funding for heating and energy assistance through LIHEAP. As a block grant, LIHEAP funds are capped at a given amount each year. The annual appropriation to the State has varied over the past five years due to decisions made at the Federal level, some of which were in response to the economic downturn.

Figure 1 displays the State's annual LIHEAP spending since fiscal year (FY) 2006-07 and the fluctuation in the availability of funds. Before the economic downturn, the annual block grant spending totaled \$111.9 million. By FY 2009-10, the availability of additional Federal LIHEAP funding had peaked, which made it possible for the State's spending to more than double. While the State's projected appropriations in FY 2013-14 and FY 2014-15 are still more than 30.0% greater

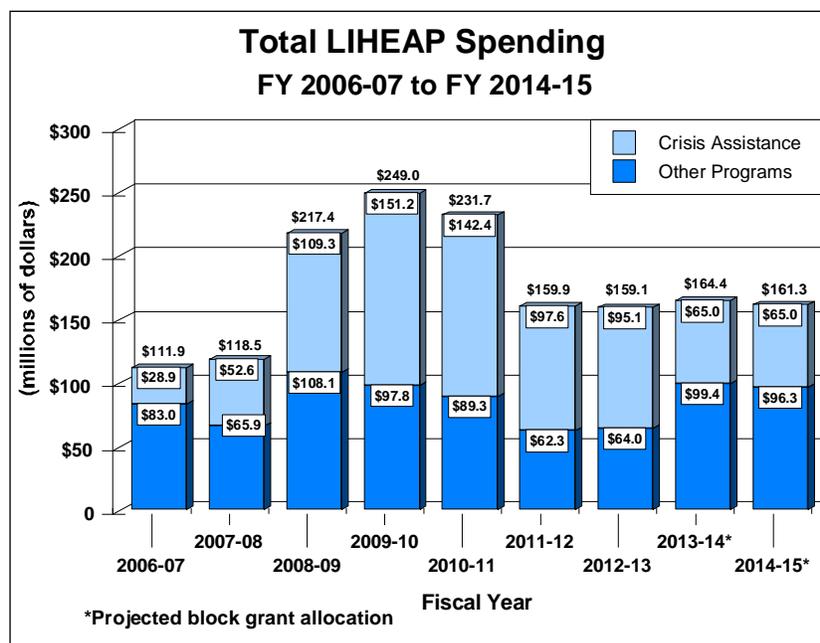
¹ Data provided by the Michigan Department of Human Services.



than FY 2006-07 levels, the amount of Federal funding that was appropriated nationwide is less than half of the amount that was available at the peak in FY 2009-10.² The Federal funding is expected to continue to decline.

The total amount of LIHEAP block grant funding that Michigan received in FY 2013-14 was \$164.4 million. At \$156.3 million, the State's FY 2013-14 year-to-date spending is lower than the amount available. The end-of-year book-closing adjustments have not yet been finalized, however, so it is unclear whether the State will have excess LIHEAP funding available to fund additional program objectives, such as Heat and Eat, or to carry forward into FY 2014-15. While the enacted FY 2014-15 State budget includes \$175.0 million in LIHEAP funding, the projected total block grant is \$161.3 million.³

Figure 1



Source: MAIN and Department of Human Services Trend Reports

The State has used LIHEAP funding to support several energy programs for low-income individuals: energy crisis assistance, Heat and Eat, Home Heating Credit, Michigan Energy Assistance Program, and weatherization, as well as administrative overhead costs.⁴ Figure 1 shows that much of the LIHEAP funding is directed to crisis assistance, which primarily helps low-income residents with heating and energy bills to avoid shutoffs during the winter months.

² Federal LIHEAP funding totaled \$8.5 billion in FY 2009-10, and \$3.6 billion in FY 2013-14. "Low-Income Energy Programs Funding History 1977-2014", Department of Health and Human Services LIHEAP Clearinghouse. http://liheap.ncat.org/Funding/energyprogs_hist.htm.

³ Part of the funding has been released in the LIHEAP Initial Continuing Resolution Release of Block Grant Funds. <http://www.acf.hhs.gov/programs/ocs/resource/liheap-2014-cr-release>.

⁴ Previous Senate Fiscal Agency *State Notes* articles on low-income energy assistance provide additional information on other energy programs and sources of funding: "State Faces Reduced Funding for Low-Income Energy Assistance Programs in Winter 2011-12" (Fall 2011 issue), and "Development of the Michigan Energy Assistance Program and Low-Income Energy Assistance Fund" (Winter 2014 issue). <http://www.senate.michigan.gov/sfa/Publications/Notes/notes.html>.

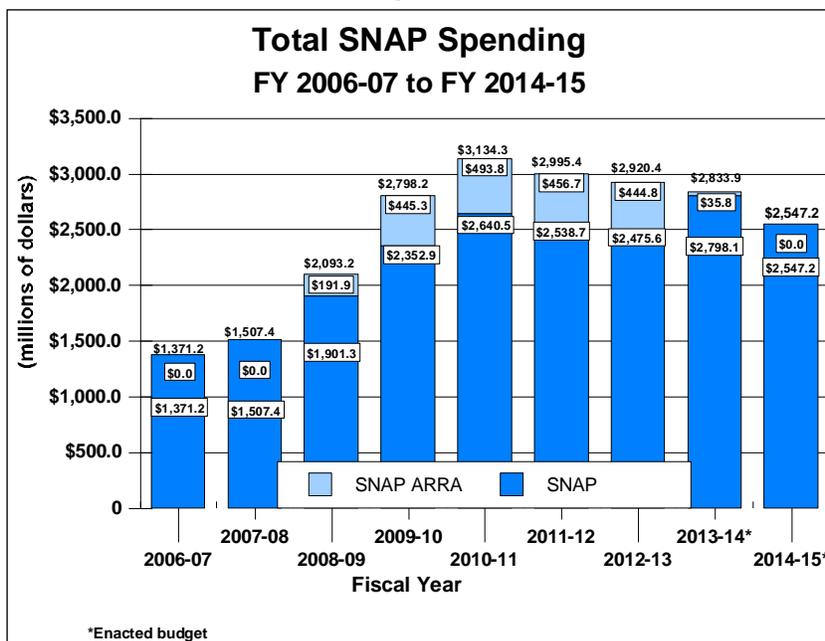


When Federal funding peaked in FY 2009-10, the average monthly caseload for energy crisis assistance was 31,662 cases with a monthly cost of \$15.1 million. The average payment for each case receiving crisis assistance was \$334. In FY 2013-14, the year-to-date monthly caseload average is 16,467 at an average monthly cost of \$6.0 million. The average benefit for each case receiving crisis assistance is \$268.⁵ The decline in the crisis assistance caseload is due to several factors, such as changes in program eligibility, the launch of an energy self-sufficiency program, and the reduced availability of Federal funding.

Supplemental Nutrition Assistance Program: The Supplemental Nutrition Assistance Program (SNAP) is the Federal food assistance program, which is provided to the states through the U.S. Department of Agriculture. SNAP is commonly referred to as food stamps.⁶ The Federal government determines most of the eligibility requirements and payment levels for individuals who are enrolled in the State's Food Assistance Program in order to receive SNAP assistance.

Figure 2 shows that the availability of Federal SNAP funding peaked in Michigan in FY 2010-11 at \$3.1 billion, an increase of 129.0% over pre-economic downturn funding levels in FY 2006-07. This increase is partially due to an increased caseload. At the peak in FY 2010-11, the average monthly FAP caseload was 967,566 and each case received an average payment of \$270 per month. In FY 2013-14, the year-to-date average monthly FAP caseload is 874,799 (or 1,685,071 individuals, 41.0% of whom are children), a decrease of approximately 9.0%. The average case currently receives \$245 per month.⁷

Figure 2



Source: MAIN

⁵ Michigan Department of Human Services Trend Reports.

⁶ The term "food assistance" is more technically accurate than "food stamps", however, as it is used in Federal law.

⁷ Michigan Department of Human Services Trend Reports.



Part of the increased funding came from the American Recovery and Reinvestment Act (ARRA). This funding became available in FY 2008-09 and provided additional monthly assistance to recipients. The FY 2014-15 enacted budget for the DHS includes \$2.5 billion in SNAP funding, which is lower than the peak levels, yet 86.0% higher than FY 2006-07 levels.

Poverty Rate in Michigan

The increase in Federal funding during the economic downturn corresponded to an increase in the poverty rate in the State. For reference, the Federal poverty level for a family of four was \$20,000 in 2006; \$22,050 in 2010; and \$23,550 in 2013.⁸

Table 1 demonstrates that the poverty rate in Michigan increased more rapidly than the national average from 2006 to 2013.

Table 1
Comparison of Poverty Rate

Year	Michigan	Nationwide
2006	13.5%	13.3%
2010	16.8%	15.3%
2011	17.5%	15.9%
2013	17.0%	15.8%

Source: U.S. Census Bureau, American Community Surveys⁹

Standard Utility Allowance

The Standard Utility Allowance (SUA) in the Food Security Act of 1985 allowed the states to claim additional SNAP assistance for households that received any amount of LIHEAP funding. In effect, the states were able to provide LIHEAP payments in any amount, including \$1, to households in order to draw down additional monthly food assistance payments for SNAP cases that otherwise would not have qualified for the additional assistance.

In order to determine the amount of SNAP assistance for which a case is eligible, states are allowed to use various income deductions. The monthly food assistance payment that is provided to a case will increase as income decreases (or as the number of income deductions increases). Deductions might include excess medical expenses, earned income, dependent care, and utility and heating costs. The Federal Food and Nutrition Service (FNS) approves the income deductions that states use to determine the payment levels. The Federal government allows states to use a standard deduction for heating and utility costs, in order to simplify the administrative process. Under previous Federal law, the State was able to apply an automatic standard deduction for heat and utilities (known as the Standard Utility Allowance, or SUA) to all cases that received any amount of LIHEAP. This standard deduction resulted in approximately \$76.73 more per month in food assistance for 18.2% of the FAP caseload, which allowed the households to spend earned income on other needs, such as rent and utilities.

⁸ "HHS Poverty Guidelines", Department of Health and Human Services. [http:// aspe.hhs.gov/poverty](http://aspe.hhs.gov/poverty).

⁹ "Percentage of People With Income Below Poverty Level in the Past 12 Months by State: 2000 to 2012", U.S. Census Bureau. <http://www.census.gov/prod/2013pubs/acsbr12-01.pdf>. Also, "Number and Percentage of People in Poverty in the Past 12 Months by State and Puerto Rico: 2012 and 2013", U.S. Census Bureau. <http://www.census.gov/content/dam/Census/library/publications/2014/acs/acsbr13-01.pdf>.



More than 81.0% of the State's FAP recipients are eligible for the standard utility deduction under both the old and the new rule. Some recipients, however, live in rental homes where heat and utilities are not separate expenses and, rather, are rolled into the monthly rent payment. In these cases, many recipients do not have documentation showing that they pay for these expenses. Some renters retain eligibility for the SUA if their landlords provide a letter indicating that they pay excess heating or cooling costs as part of their rent payments. Under previous Federal law, the State had implemented an automatic SUA for all cases, including these renters. These households will not necessarily be eligible for the standard deduction in the future, however.

Agricultural Act of 2014

With the changes implemented in the Agricultural Act of 2014, which went into effect in Michigan on May 1, 2014, the State will no longer automatically apply the SUA to all FAP cases. This Act requires a minimum level of over \$20 in LIHEAP assistance in order for households to claim an income deduction for utility costs when SNAP benefits are calculated.

The Supplemental Nutrition Assistance Program was reauthorized as part of the Agricultural Act of 2014, which affected some of the rules regarding eligibility, benefits, and administration. Section 4006 states: "[I]f a State agency elects to use a standard utility allowance that reflects heating and cooling costs, the standard utility allowance shall be made available to households that received a payment, or on behalf of which a payment was made, under the Low-Income Home Energy Assistance Act of 1981 (42 U.S.C. 8621 et seq.) or other similar energy assistance program, if in the current month or in the immediately preceding 12 months, the household either received such a payment, or such a payment was made on behalf of the household, that was greater than \$20 annually, as determined by the Secretary."

With the change in Federal statute, the Heat and Eat policy is in question. For example, the Chairperson of the U.S. Senate Committee on Agriculture, Nutrition & Forestry, Michigan Senator Debbie Stabenow, characterized the Heat and Eat policy on the Committee website in the following way: "The 2014 Farm Bill achieves virtually all of its \$8 billion in nutrition program savings by addressing a program misuse, commonly referred to as 'heat and eat,' whereby a small number of states are artificially inflating some people's food assistance benefits by **listing a utility bill they don't actually have** on their food assistance applications [emphasis in original]."¹⁰

Additionally, the DHS has cited a number of concerns regarding eligibility standards in Federal statute that may conflict with the Heat and Eat policy. First, Section 2602 of the Low-Income Home Energy Assistance Program Act of 1981 authorizes grants to states in order to "assist low-income households, particularly those with the lowest incomes, that pay a high proportion of household income for home energy, primarily in meeting their immediate home energy needs". The concern is that the Heat and Eat policy would provide LIHEAP funding to households with no actual heating costs. Next, Federal LIHEAP eligibility criteria allow payments for those who are at 150% of the Federal poverty level, while SNAP recipients may qualify for assistance if their income is at 200% of

¹⁰ <http://www.ag.senate.gov/newsroom/press/release/2014-farm-bill-addressing-misuse-protecting-food-assistance>



the Federal poverty level. Other concerns include potential audit findings due to these statutory conflicts, as well as possible administrative complications.¹¹

Nonetheless, the Agricultural Act of 2014 does permit the states to provide a minimum \$20.01 LIHEAP payment for SUA eligibility, rather than eliminate the option entirely. Additionally, the Federal government had reviewed and approved Michigan's annual LIHEAP State Plan, which included the Heat and Eat policy, for several years, declining to reject the proposal based on any of the concerns that were cited. Despite the outstanding questions, some states are continuing the policy, while others have discontinued it.

Heat and Eat in Other States

Previously, 16 states and the District of Columbia had used some variation of a Heat and Eat policy in order to increase SNAP benefits for some households.¹² The states were California, Connecticut, Delaware, Maine, Massachusetts, Michigan, Montana, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, Vermont, Washington, and Wisconsin. New Hampshire had implemented a modified version of the program.¹³

Based on the most recent available information, four of the 16 states will not continue the program: Michigan, New Hampshire, New Jersey, and Wisconsin. The remaining 12 states and the District of Columbia will use various mechanisms to continue the program, including updating policy, changing state statute, or increasing General Fund/General Purpose (GF/GP) funding.¹⁴ The various implementation paths suggest that the states are not in agreement on how the Federal rules and statutes should be applied.

Some examples suggest that the programs will apply the SUA only to cases that otherwise would not qualify. For example, at approximately 1.7 million, New York's food assistance caseload is much higher than Michigan's but the program is tailored to assist just 300,000 households at a cost of \$6.0 million.¹⁵

Similarly, California has a food assistance caseload of more than 2.0 million, yet the budget includes funding to continue the SUA for just 320,000 households. California will implement a variation on the

¹¹ Another potential conflict that was not cited by the DHS is in U.S. Code, Title 7, Chapter 51, Section 2014, which defines eligible households. The section states that the SUA cannot be used for a household that "does not incur a heating or cooling expense, as the case may be;" or for households that reside in public housing that uses central meters. This rule potentially could conflict with any attempts to provide the SUA to households where residents are renting and also do not have some kind of documentation of unique heating or cooling expenses.

¹² Aussenberg, Randy Alison and Perl, Libby. *The 2014 Farm Bill: Changing the Treatment of LIHEAP Receipt in the Calculation of SNAP Benefits*. Congressional Research Service, 2014. http://www.ncsl.org/Portals/1/Documents/cyf/2014FarmBill_LIHEAP.pdf.

¹³ *A New Framework for Heat and Eat: LIHEAP and SNAP After the 2014 Farm Bill*. LIHEAP Clearinghouse Issue Brief, August 2014. <http://www.liheap.ncat.org/pubs/LCIssueBriefs/heateat/HeatEat.pdf>.

¹⁴ Mendoza, Gilberto Soria. *Heat and Eat and SNAP Changes in the 2014 Farm Bill*, National Conference of State Legislatures, 2014. <http://www.ncsl.org/research/human-services/-heat-and-eat-and-snap-changes-in-the-2014-farm-bill.aspx#HEAT AND EAT>.

¹⁵ Cuomo, Andrew M. *Governor Cuomo Announces New York State Will Preserve \$457 Million in Snap Benefits for 300,000 Households*, February 25, 2014. <https://www.governor.ny.gov/press/02252014-snap-benefits>.



Heat and Eat policy, funding it with GF/GP dollars rather than LIHEAP funds. This approach will maintain the amount of funding that is available for heating and cooling assistance. The FY 2014-15 enacted budget for the State of California included \$10.5 million GF/GP for the State Utility Assistance Subsidy. This new state-funded energy assistance program will offset the LIHEAP funding that is designated to pay the \$20.01 minimum for extended food assistance. The state estimates that the program will increase household monthly food budgets by an average of \$62.¹⁶

In contrast, Pennsylvania's approach suggests that the SUA will be applied to every LIHEAP household, as opposed to only the cases that stand to lose benefits. Pennsylvania estimates that \$8.0 million in LIHEAP funding will serve 400,000 households. The average monthly increase in SNAP benefits will be in the range of \$60 to \$65.¹⁷ Pennsylvania's food assistance caseload is similar in size to Michigan's. In July 2014, Pennsylvania served 898,623 cases.

Michigan's Policy Change and Impact

The State of Michigan's decision to discontinue funding for the Heat and Eat policy will affect approximately 18.2% of the total FAP caseload, or approximately 159,000 cases. The FY 2013-14 average monthly FAP caseload is 873,048. The monthly reduction in benefits for the cases that no longer qualify for the SUA will vary based on the number of people in the case, with an average reduction of \$76.73. The estimated total annual reduction in SNAP funding throughout the State could be as much as \$146.4 million, or 5.0% of the total \$2.5 billion projected funding in FY 2014-15.

The Department of Human Services currently estimates that the costs to continue the policy would be \$18.5 million.¹⁸ This estimate assumes that \$21 would be provided to every FAP case (873,048) rather than every LIHEAP household (approximately 450,000). Using this estimate, the result could be that as many as 69,000 fewer payments would be made for energy crisis assistance or energy self-sufficiency services through the Michigan Energy Assistance Program, which are funded by LIHEAP revenue. As previously discussed, however, the states that are continuing the Heat and Eat policy are approaching the SUA eligibility from different methods.

If Michigan were to apply the SUA in a way that was similar to the approaches in New York or California, the costs would be much lower than this estimate.¹⁹ If the 18.2% of FAP cases that otherwise will lose the extended benefits received \$21 to qualify for the SUA, the costs would be approximately \$3.3 million. In this scenario, the result could be that approximately 12,300 fewer payments would be made for low-income energy assistance.

If Michigan were to apply the SUA to LIHEAP households in a way that was similar to Pennsylvania's program, the costs would fall in the middle of the other estimates. It would cost approximately \$9.5 million to provide 450,000 households with \$21. This estimate also aligns with the previous

¹⁶ California Enacted State Budget Summary, 2014-15. Health and Human Services Budget.
<http://www.ebudget.ca.gov/2014-15/pdf/Enacted/BudgetSummary/HealthandHumanServices.pdf>.

¹⁷ Buhrig, Cathy. *The SNAP LIHEAP Connection*, Pennsylvania Department of Public Welfare, 2014.
<http://liheap.ncat.org/pubs/LCIssueBriefs/heateat/PAWelfareDept.pdf>.

¹⁸ Early estimates from the DHS placed the total cost at approximately \$20.0 million to \$26.4 million (16.0% of the total LIHEAP block grant).

¹⁹ LIHEAP assistance is provided per household, which means that the caseload is smaller than the food assistance caseload, as multiple food assistance cases can exist under the same roof. Section 2603 of the Low-Income Home Energy Assistance Act of 1981 defines "household" as "any individual or group of individuals who are living together as one economic unit for whom residential energy is customarily purchased in common or who make undesignated payments for energy in the form of rent".



expenditures under the State's \$1 LIHEAP program from 2010 to 2014, which affected between 400,000 and 475,000 households. If \$9.5 million were spent on Heat and Eat, the result could be that approximately 35,000 fewer payments would be made for low-income energy assistance.

As discussed above, over 81.0% of the FAP caseload will retain eligibility for the SUA and increased food assistance. Some clients will be able to verify that they have received more than \$20 in LIHEAP funds for other energy programs, such as the Home Heating Credit, in either the month of application or within the prior 12 months. This proof will allow them to qualify for the expanded food assistance benefits. Clients also may qualify by demonstrating sufficient heating or cooling expenses regardless of LIHEAP assistance.

Conclusion

The Federal government is funding both LIHEAP and SNAP at higher levels than those available before the economic downturn. At the same time, the State's poverty rate has not yet returned to pre-economic downturn levels and remains higher than the nationwide average. While many states are opting to continue the Heat and Eat policy under the new Federal requirements, the DHS has expressed concerns regarding possible conflicts with Federal statute. In order to continue the program at the previous levels, providing \$21 rather than \$1 to 450,000 households, the State would have to spend approximately \$9.5 million. While the caseload for energy crisis assistance continues to decline, possibly leaving the State with unspent funding at the end of the year, the Federal LIHEAP funding also is beginning to decline. If Michigan were to continue the Heat and Eat policy at the increased cost, this decision could result in a reduction in the amount of funding that is available for low-income energy assistance programs.