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The Proposed Executive Budget, Fiscal Year 1985-86

For the third time in as many years the governor has recommended a constrained state budget. Under the governor's proposal, general fund-general purpose (GF-GP) outlays would increase by 3.2% (\$5.651 billion v. \$5.474 billion) above currently authorized spending levels for fiscal year 1984-85. Total state budget outlays would increase by 6.0% (\$13.570 billion v. \$12,726 billion) over authorized 1984-85 levels. After adjustment for the estimated rate of inflation, the purchasing power of the GF-GP budget would contract by approximately 0.8%, while that for the total state budget would increase by roughly 2%.

The 1985-86 budget would perpetuate the shift in funding toward education and away from income maintenance programs such as aid to families with dependent children (AFDC) and general assistance (GA). A summary of proposed GF-GP spending amounts by department or budget area is presented in the table following.

If pending or anticipated requests for additional funding are approved for the current fiscal year, GF-GP funding for three budget areas--school aid, the

Department of Labor, and the Department of Social Services--would be less in 1985-86 than the 1984-85 postsupplemental levels. Absent supplemental appropriations, only two budget areas--the Library of Michigan, and the Department of Labor--would experience actual declines in the total number of dollars available for their use next year. Costs for debt service would also decline during the next fiscal year, largely because the state expects to borrow only \$300-\$350 million, considerably less than the \$450 million borrowed during this fiscal year.

The funds to be cut from the Department of Social Services would be redistributed to other programs and departments. The largest dollar increase would go for higher education institutions and programs: community colleges would receive a 7.5% GF-GP increase worth \$11.9 million, and state colleges and universities would receive a 12.5% increase worth \$105.4 million. In addition to a base increase of \$39.5 million (5.0%) for the state colleges and universities, the budget request includes \$25.0 million for a new research excellence fund, \$15.8 million for tuition stabilization, and the

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General Fund-General Purpose Budget Summary Fiscal Years 1984-85 and 1985-86

Department or Program	Authorized FY 1984-85 Appropriations ^a	FY 1985-86 Executive Recommendations	Increase or Decrease over FY 1984-85	% Change
HUMAN SERVICES				
Social Services	\$2,075,918,800	\$1,950,276,526	- \$125,642,274	- 6.0
Mental Health	593,575,800	649,913,354	+ 56,337,554	+ 9.5
Public Health	109,051,300	123,597,600	+ 14,546,300	+ 13.3
Corrections	292,484,100	315,283,300	+ 22,799,200	+ 7.8
EDUCATION				
Education	30,672,800	38,202,975	+ 7,530,175	+ 24.4
School Aid	481,047,000	440,123,200	- 40,923,800 ^b	- 8.5
Community Colleges	159,307,300	171,236,600	+ 11,929,300	+ 7.5
State Colleges and Universities	845,955,600	951,350,400	+ 105,394,800	+ 12.5
Library of Michigan	18,026,800	18,824,400	+ 797,600	+ 4.4
GENERAL GOVERNMENT				
Executive Office	3,188,400	3,474,400	+ 286,000	+ 9.0
Legislature	57,423,800	60,167,500	+ 2,743,700	+ 4.8
Judiciary	67,737,500	78,860,600	+ 11,123,100	+ 16.4
Attorney General	18,343,500	20,235,500	+ 1,892,000	+ 10.3
State	10,242,800	15,526,400	+ 5,283,600	+ 51.6
Management and Budget	98,773,700	121,329,800	+ 22,556,100	+ 22.8
Treasury	56,298,300	59,126,700	+ 2,828,400	+ 5.0
Civil Rights	9,592,000	9,794,400	+ 202,400	+ 2.1
Civil Service	9,784,500	10,449,000	+ 664,500	+ 6.8
REGULATORY				
Commerce	72,279,500	82,039,000	+ 9,759,500	+ 13.5
Labor	30,168,300	31,514,800	+ 1,346,500	+ 4.5
Licensing and Regulation	14,170,500	15,269,200	+ 1,098,700	+ 7.8
SAFETY AND DEFENSE				
State Police	143,281,800	148,969,100	+ 5,687,300	+ 4.0
Military Affairs	10,638,000	11,286,440	+ 648,440	+ 6.1
AGRICULTURE AND NATURAL RESOURCES				
Agriculture	24,330,700	25,849,700	+ 1,519,000	+ 6.2
Natural Resources	84,912,100	110,804,800	+ 25,892,700	+ 30.5
OTHER				
Transportation ^c	- 0 -	- 0 -	- 0 -	- 0 -
Capital Outlay	69,678,000	107,473,700	+ 37,795,700	+ 54.2
Debt Service	87,530,500	80,183,700	- 7,346,800	- 8.4
TOTAL^d	\$5,474,413,400	\$5,651,163,095	+ \$176,749,695	+ 3.2

SOURCE: Governor Blanchard's Proposed FY 1985-86 Budget, Senate Fiscal Agency, February 7, 1985, and Budget Message of the Governor, 1985-86 Fiscal Year.

^aExcludes anticipated supplemental appropriations of approximately \$58 million in fiscal year 1984-85.

^bThe General Fund compensates for shortfalls between school aid appropriations and revenues reserved for school aid funding. School aid revenues are projected to increase by \$178,590,200 in fiscal year 1985-86, so the requirements from the General Fund will decline.

^cThe Department of Transportation relies on transportation taxes and federal funds for its budget and hence receives no General Fund appropriations. Total dollars available to the department would, under the fiscal year 1985-86 executive budget projections, increase 5% or \$3,882,100 over fiscal year 1984-85 levels.

^dExcludes payments to the Budget Stabilization Fund of \$348.7 million in fiscal year 1984-85 and \$176 million in fiscal year 1985-86.

consolidation of the tuition differential grant program with the tuition grant program.

The smallest dollar increases would go to the Department of Civil Rights (\$202,400) and the Executive Office (\$286,000), GF-GP increases of 2.1% and 9.0%, respectively. The 2.1% increase for the Department of Civil Rights is also the smallest percentage increase for any GF-GP expenditure area.

The largest percentage increase in general fund appropriations would go to capital outlay programs, up 54.2% (\$38.0 million), and the Department of State, up 51.6% (\$5.3 million). The additional funding for capital outlay would be used primarily to maintain and remodel facilities for state colleges, universities, and community colleges and to pay for bonds to construct new prison facilities. The largest share (\$2.8 million) of the GF-GP appropriation to the Department of State would be devoted to implementing a federally required vehicle emission inspection and maintenance program in southeastern Michigan.

Although school aid would receive \$40.9 million less from the general fund during 1985-86 compared to 1984-85, total funds available for school aid use would increase by \$132.9 million (8.0%) due to an increase in the amount of state restricted funds allocated to it. The governor's proposed fiscal year 1985-86 budget would reserve to school aid the additional 10¢ tax per pack of cigarettes that has, since 1982, been reserved to the state's working capital reserve account.

This change would further insulate K-12 school aid funding from unexpected fluctuations in the availability of general fund dollars. It would also reduce the proportion of the total state budget controlled by the Michigan Legislature. If this allocation is approved, only 42% of the total state budget will be subject to control by the legislature, down from 49.8% as recently as 1980.

As in the current year, the proposed budget for 1985-86 would send more dollars to local units of government than the 41.61% share of total state spending mandated by Michigan's constitution. The \$4,325.3 million payment exceeds the amount the state is required to return to local governmental units by \$164.8 million and represents 43.26% of total recommended state spending.

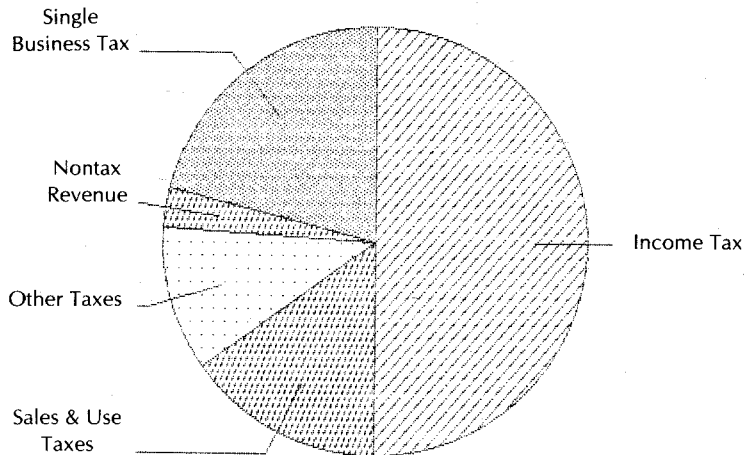
The table excludes the transfer of \$176 million from the general fund to the budget stabilization fund, approximately 3.0% of the GF-GP budget. Other factors that may impinge on the governor's recommended 1985-86 general fund budget include a possible early rollback of the temporary increase in the state income tax; a proposed increase in the personal income tax deduction from \$1,500 per person to \$1,750 per person; elimination of selected tax exemptions; and additional property tax relief. Depending on the combination of proposals to be enacted, revenues available to the state general fund could decline by approximately \$460 million, requiring corresponding reductions in general fund expenditures.

Proposed Distribution of Revenues and Expenditures, Fiscal Year 1985-86

Figures 1 through 4 illustrate the funding sources and allocations of Michigan's proposed general fund and total budget for fiscal year 1985-86. Figure 1 shows that 86% of general fund revenues would be provided by just four of the state's taxes--individual income, single business, sales, and use. Figure 3 shows that these same four taxes would provide about 53% of total anticipated state revenues.

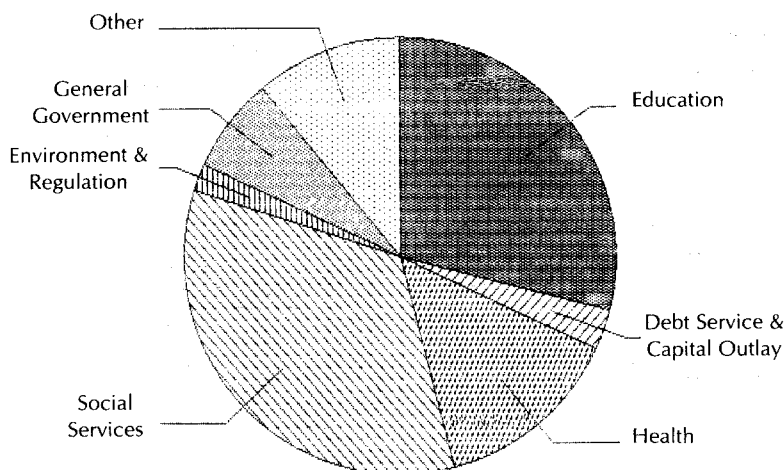
Figure 2 shows how general fund revenues would be distributed among major state program areas. As shown here, social services, health, and education together use 71¢ of every general fund budget dollar.

Figure 1
FY 1985-86 General Fund-General Purpose Projected Revenue
(Millions of Dollars)
Revenue: \$5,895.5



Revenue Sources, General Fund-General Purpose Budget	
Income Tax	50%
Single Business Tax	21%
Sales & Use Taxes	15%
Other Taxes	11%
Nontax Revenue	3%

Figure 2
FY 1985-86 Requested Expenditures, General Fund-General Purpose Budget
(Millions of Dollars)
Expenditures: \$5,651.2



Expenditure Areas, General Fund-General Purpose Budget	
Social Services	34%
Education	29%
Health	14%
General Government	7%
Environment & Regulation	2%
Debt Service & Capital Outlay	3%
Other	11%

Figure 4 shows how budget dollars, from both restricted and unrestricted revenue sources, would be allocated among various state governmental functions. Education would receive 30¢ of every budget dollar, while social services would obtain 32¢, transportation 9¢, health 9¢, environment and regulation 2¢, with remaining state programs competing for the other 18¢ of the state budget dollar.

Budget Trends during the Past Decade

Figures 5 and 6 show how budget priorities have changed during the last ten years. The recommendations for general fund and total state spending in 1985-86 are compared to 1980-81 and 1975-76 expenditures. Since fiscal year 1982-83 when the Blanchard administration assumed office, GF-GP dollars spent for education have increased from \$1.33 billion to \$1.62 billion (21.5%) while total budget dollars devoted to education have grown to \$4.00 billion from \$3.01 billion (32.9%). However, as the figures show, most of the increase is attributable to growth in the size of the general fund and total state budgets, since the share of budget dollars allocated to education has remained relatively constant. In fiscal year 1975-76 education accounted for 39.2% of the GF-GP budget compared to the 28.7% proposed for fiscal year 1985-86. Similarly, total expenditures for education represented 30.1% of the budget in 1975-76, almost unchanged from the 29.7% share proposed for fiscal year 1985-86.

Funding for prenatal care programs would more than double in fiscal year 1985-86, although total health care funding from general fund sources would rise by 10.0% (6.6% on the basis of total funding) compared to the current year. Despite these increases, total funding for public and mental health programs has remained relatively constant over the 10-year period.

Several other facts emerge from these figures. Much attention has been focused

on the size of the welfare caseload and on the dollars devoted to income support programs, but the share of the budget used for income support has changed very little over the past 10 years regardless of the strength or weakness of the state's economy and tax revenue levels.

Increased awareness and concern for environmental protection and safe toxic waste disposal has stimulated more state and federal spending for these particular programs. Spending for environmental and regulatory programs would account for 2.1% of the total 1985-86 state budget compared to only 1.8% in fiscal year 1975-76.

Finally, state government has broadened its responsibilities. While the domain of state involvement once principally included only highway construction, public safety, and human service programs, an increasing share of the state's energies and resources has been used to support a wide variety of additional programs and initiatives, as can be seen by the increases in state budget dollars going to "other" areas.

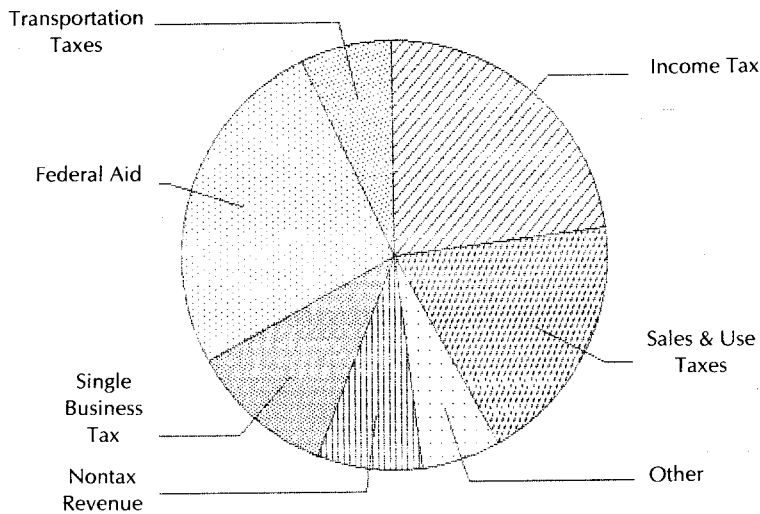
Assumptions of the 1985-86 Fiscal Year Budget

Budget plans can be no more accurate than the revenue and economic assumptions upon which they are based. The 1985-86 budget proposal anticipates that the national and state economies will grow at respectable rates during calendar years 1985 and 1986 but well below the growth rates of 1984. The governor projects that total U.S. auto sales will decline by 200,000 to 10.2 million units and that consumer prices will rise at 6.2% compared to 4.5% this year. The national unemployment rate will decline from 7.3% to 7.1%; and the Michigan unemployment rate will decline from 7.7% to 7.2%. Michigan personal income is also projected by the governor to increase by 7.2% in 1986.

The probable consequence of both an increase in personal income and a reduction in the unemployment rate will be a

Figure 3

FY 1985-86 Projected Revenue, Total State Budget
(Millions of Dollars)
Revenue: \$13,777.5

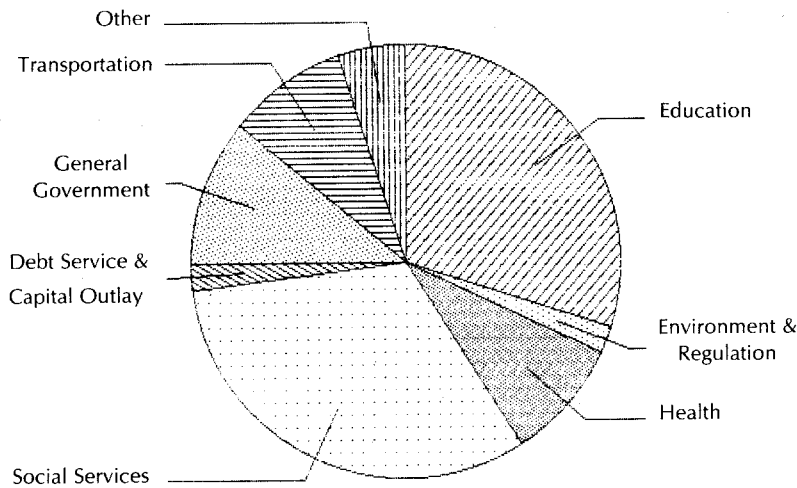


Revenue Sources, Total State Budget

Federal Aid	26%
Income Tax	23%
Sales & Use Taxes	19%
Single Business Tax	11%
Transportation Taxes	7%
Nontax Revenue	8%
Other	6%

Figure 4

FY 1985-86 Requested Expenditures, Total State Budget
(Millions of Dollars)
Expenditures: \$13,463.3



Expenditure Areas, Total State Budget

Social Services	32%
Education	30%
General Government	11%
Transportation	9%
Health	9%
Environment & Regulation	2%
Debt Service & Capital Outlay	2%
Other	5%

decline in AFDC and GA caseloads. The governor's proposed budget projects that the average monthly AFDC caseload level will drop by 6.7% to 215,000 cases while the GA caseload will decline by 15.8%, reflecting both improvements in employment (14,666 cases) and participation in the Community Service Corps (7,300 cases). The proposed budget does not incorporate the possibility of an expanded personal income tax exemption or accelerated rollback of the temporary income tax increase.

FAS Commentary

The economic assumptions on which the governor's budget request is based are somewhat more pessimistic than our projections of economic performance during 1986. (See our economic forecasts of November 1984 and March 1985.) However, the administration's estimate of yield from the major state taxes is somewhat higher than our estimates. The net result is that the two estimates of total available revenues correspond closely. This seems reasonable in light of current economic conditions.

At \$5,895.5 million, projected FY 1985-86 GF-GP revenues will exceed requested GF-GP expenditures by \$244 million. Of this amount, \$176 million will be transferred to the budget stabilization fund, leaving a net surplus of \$68 million. The Blanchard administration has recommended using this surplus for additional property tax relief.

Revenues from all sources are projected at \$13,777.5 million with requested expenditures totaling \$13,363.3 million, leaving a surplus of \$31.4 million or approximately 2.3% of total state revenues. This is a razor-thin operating surplus and provides little room either to cut taxes or to extend tax relief.

Since 1986 is a major state election year, the political desire for reducing the tax burden is understandable. Policy-

makers, however, should balance the political efficacy of their actions against the long-term stability and financial integrity of the state. As we enter the fourth consecutive year of positive economic growth, we are only now beginning to reverse the damage that the last recession wrought on our programs and institutions. This progress came too hard and at too high a price to sacrifice it to short-term political interests.

Of equal concern is the tendency to reduce the discretionary portion of the state budget. Since 1977, three factors have combined to constrain legislative control of the general fund-general purpose budget: (1) establishment of the budget stabilization fund, (2) adoption of the so-called Headlee amendment to the constitution, and (3) dedication of state revenues for the exclusive use of selected programs. All three factors reduce the amount of dollars available to the general fund, but the last two also restrict the way in which state funds can be spent.

Despite the considerable restraints placed on the budget process through the budget stabilization fund and the Headlee amendment, there has been considerable impetus to erode further the ability of the legislature to allocate and spend budget dollars. The governor's proposed 1985-86 fiscal year budget perpetuates this trend by recommending that the 10¢ per pack cigarette tax currently used to bolster the state's cash reserves be dedicated to school aid funding. While this would help insulate financial aid to local K-12 school districts from the ravages of a recession-induced decline in general fund revenues, it further reduces the share of the budget dollars over which the legislature has discretionary control. This means that if spending must again be cut at some point in the future, the burden of reductions will be spread over fewer programs, intensifying the hardship on those portions of the budget whose funding is not protected--e.g., higher education, social services, public and mental health, corrections, and public safety.

Figure 5
Comparison of
General Fund Expenditures
1985-86, 1980-81, 1975-76

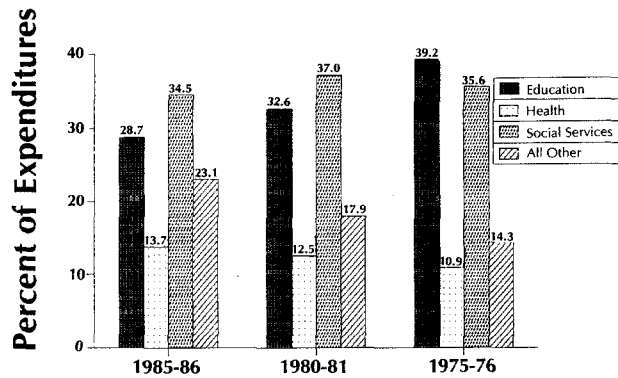
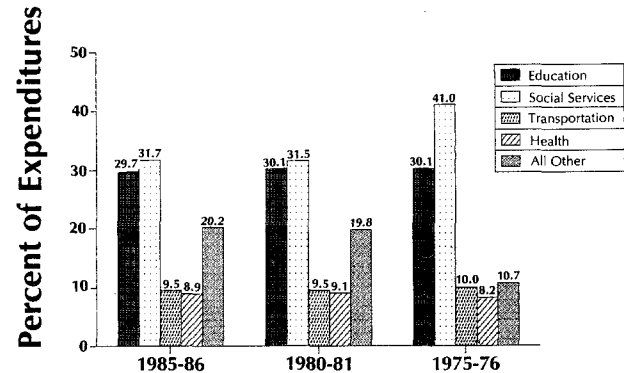


Figure 6
Comparison of
Total State Budget Expenditures
1985-86, 1980-81, 1975-76



Since Michigan's economy is highly vulnerable to the fluctuations of the business cycle, the trend toward protecting the funding of selected programs seems to us to portend increased hardship during the next recession for postsecondary education institutions and for public safety and entitlement programs. While guaranteed funding for K-12 education has great surface appeal, those who develop and implement budget policy must seriously consider the consequences of increased dedication of tax revenues for the sole use of education or any other budget area.

The role of state government is to provide a broad range of public services to all residents. Dollars can be spent only once; funds used to support one program may not subsequently be used to support other programs. It would be unfortunate if the public officials of this state, in their desire to protect one area of the budget over others, jeopardized the ability of Michigan's government to respond equitably and appropriately to the changing needs and concerns of the general public. The trend toward reducing the discretionary portion of the state budget could have precisely that effect.

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