



# KELLEY CAWTHORNE

## CAPITOL REPORT

November 1, 2007

The Michigan Legislature early Halloween morning (Wednesday, October 31<sup>st</sup>) finally resolved the state's 2007-08 **budget battle** by sending the last of 17 budget bills on to Governor Granholm for her signature.

Bolstered by nearly \$1.4 billion in controversial **new taxes** approved just a month ago, lawmakers enacted a \$9.862 billion general fund budget that actually exceeds the 2006-07 general fund budget by \$750 million. A good chunk of that number, however, reflects 2008 payment of \$329 million owed to institutions of higher learning that went unpaid in 2007.

Also included in the \$750 million general fund increase is \$165.8 million in higher **Medicaid** spending, \$147 million in additional state employee wages and benefits, nearly \$20 million in increased debt service and \$90 million that previously was paid out of an earmarked (Merit Award) trust fund.

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So what about the \$435 million in **spending cuts** that was supposed to be part of the 2007-08 budget solution? Turns out that number was reached by using a "current services" budget that assumes the exact same set of services (though not costs) as contained in the last budget and then cutting \$435 million from that. In other words, according to legislative budget makers, the increased cost of services rendered doesn't count when figuring the amount of a budget cut, only the value of services reduced. (Got that?) Little wonder some observers think the amount of the income tax increase and service tax is all too "real" while the much bally-hoed budget cuts are "phantom."

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In any event, **K-12 and intermediate school districts**, over-all, get a 1% increase over the past fiscal year, totaling \$199 million dollars. Medicaid, state police patrols, and secretary of state branch offices were largely spared.

The fiscal blueprint, however, closes three prisons and a prison camp and two State Police crime labs; cuts money for middle school science and math; slashes spending for some public health programs such as early hearing screening; and reduces outlays for day care services for low-income working parents and state aid to local libraries.

The budget also assumes passage of increases in hunting and fishing license fees and **environmental permits** that help foot the bill for the departments of natural resources and environmental quality. If lawmakers fail to approve the increases by Jan. 15, 2008 (and they may not) deep cuts will be made in both departments – including closing state fish hatcheries and turning over environmental permitting to the federal government.

Any euphoria over finally resolving what had been a \$1.75 billion deficit will be short-lived, fiscal experts say. Tom Clay, former state budget official and analyst for the independent Citizens Research Council of Michigan, says rapidly increasing state costs, particularly in health care, will quickly outpace state revenue increases.

“We’re going to continue to have the same problems we have been having,” Clay says. “The rate of growth in revenues is less than the growth in spending pressures. By 2009, they’ll have another half-billion-dollar spending gap” and it could be even more if the state economy doesn’t recover soon, Clay notes.

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Some budget highlights:

**Education** – Public schools, community colleges and state universities are relative winners in the budget. The minimum school aid grant for public schools will increase to \$7,204 per student. The lowest-spending school districts will get an additional \$96; the highest-spending districts will get \$48 in an attempt to achieve greater equity in school funding.

In higher education, the Legislature created a separate major research category for the University of Michigan, Michigan State University and Wayne State University. Those colleges won’t get additional funding this year, but the special status could net them more money in the future as the state tries to develop a collaborative research triangle that leads to economic development and job creation. The 15 state universities get a 1 percent increase, or \$14 million, but they were trimmed by \$26 million in last year’s cuts so they’re still behind where they were a year ago. August payments totaling \$139 million were withheld from the universities but are restored in this budget.

Tuition grants to private college students are in the budget at \$56.7 million, down \$2.1 million from last year. It remains possible that Gov. Granholm will veto the program, however. 28 community colleges will get \$3419 million, which is 1 percent above last year.

**Corrections** – The Corrections budget balloons to \$2.1 billion, an increase of better than 6 percent even though there are 1,500 fewer prisoners in state lockups. The department is closing three prisons and a prison camp and reopening the Michigan Reformatory in Ionia. Some 500 inmates who have completed their minimum sentences will be placed on tethers at a cost of \$4 million.

The state will add extra bunks at eight prisons at a cost of \$8.6 million and the reimbursement program for state prisoners housed in county jails will increase by \$13.2 million. Language in the spending bill calls for a cost-benefit analysis to determine where the department can save money for the next budget year. Corrections also will look at privatizing prisoner transportation and mental health care.

**Health** – Lawmakers managed to pass the budget without kicking anyone off Medicaid health care – a major goal of the governor’s. Among the recipients proposed for cuts were 19- and 20-year-olds and relatives who care for children on Medicaid. To avoid program cuts, doctors and hospitals agreed to ante up additional fees to expand by \$60 million a hospital **quality assurance program** that will draw federal money. State officials said Medicaid eligibility could not have been saved from reductions without new fees. Part of the spending increase goes to improved rates for Medicaid health plans.

The Healthy Michigan Fund, which pays for disease prevention, smoking cessation and other programs, was mostly preserved at \$43.5 million. But \$900,000 was cut for pregnancy prevention and family planning and early hearing detection and screening among other programs. The budget assumes \$63 million in savings from cost-cutting measures such as recovery of money from the estates of long-term care Medicaid patients. Of the \$12 billion spent for community health, only \$3.1 billion comes from the state general fund; the federal government provides much of the difference.

**Transportation** – Compromise language on the question of continuing a study of the proposed Detroit River International Crossing says that the study can be completed so long as the study does “not bind the state in any way to construction or future action of any DRIC project recommendation.” The language does allow the state to acquire property in the areas where crossings could be located, so long as they do not bind the state to a crossing.

The language also says there will be legislative hearings on the study with the department presenting an accounting on the costs of the study. Supporters of a second span at the privately-owned Detroit **Ambassador Bridge**, in opposing the DRIC study, say their plan would save the state millions in construction costs and be completed more quickly. Their plan won non-binding approval of the Senate in the form of a resolution of support.

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In 2007-08, the state will spend \$9.8 billion on per-pupil foundation grants for the state’s K-12 system. Close to that is the \$8.7 billion the state will spend on

Medicaid. Several years ago, the state began spending more on prisons than on higher education. One out of three state employees now works for the Department of Corrections.

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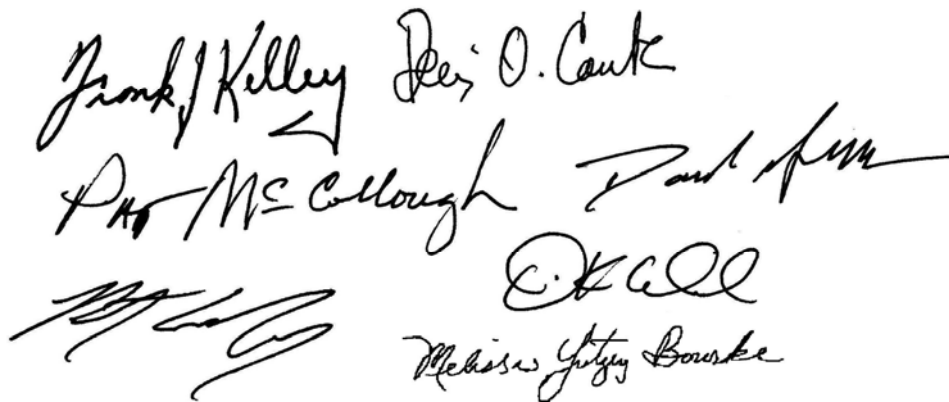
As predicted in our last newsletter (Oct. 5, 2007), legislative passage and the Governor's signature on a new 6% tax on a host of **arbitrarily selected services** -- done largely out of sight and without public input -- has kicked off a firestorm. Many legislators haven't been able to run away fast enough from what one major state law firm calculated was "the largest business tax increase in Michigan history." A broad coalition of dozens of interests groups, encouraged by some of the state's largest manufacturers, have coalesced into an "**Ax the Tax**" movement bent on repeal of the levy.

Still, it may be an **uphill battle** to get the Legislature to kill it before its scheduled December 1<sup>st</sup> implementation date. That's because lawmakers and the Governor will have to fill a \$735 million hole with other tax increases or spending cuts. As much as they may want to ditch the service tax, the prospect of going back to the well to yet again raise a tax (or to make draconian cuts to sacred spending cows), has legislators quaking in their boots.

Perhaps the least painful solution – and most doable – would be to repeal the tax and simply add a **surcharge** to the newly enacted Michigan Business Tax. But since at least a significant portion of the business community already face taxes exceeding their liability under the old SBT, the effort to add to their burden doesn't look all that enticing either.

More likely success will come from the coalition's drive to put repeal on the November 2008 ballot. An all out press in now on to get the requisite 300,000 signatures. The petition route also means, however, that the tax is almost certain to stay in place for a full year.

**Stay tuned** as the service tax repeal effort gains steam!



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