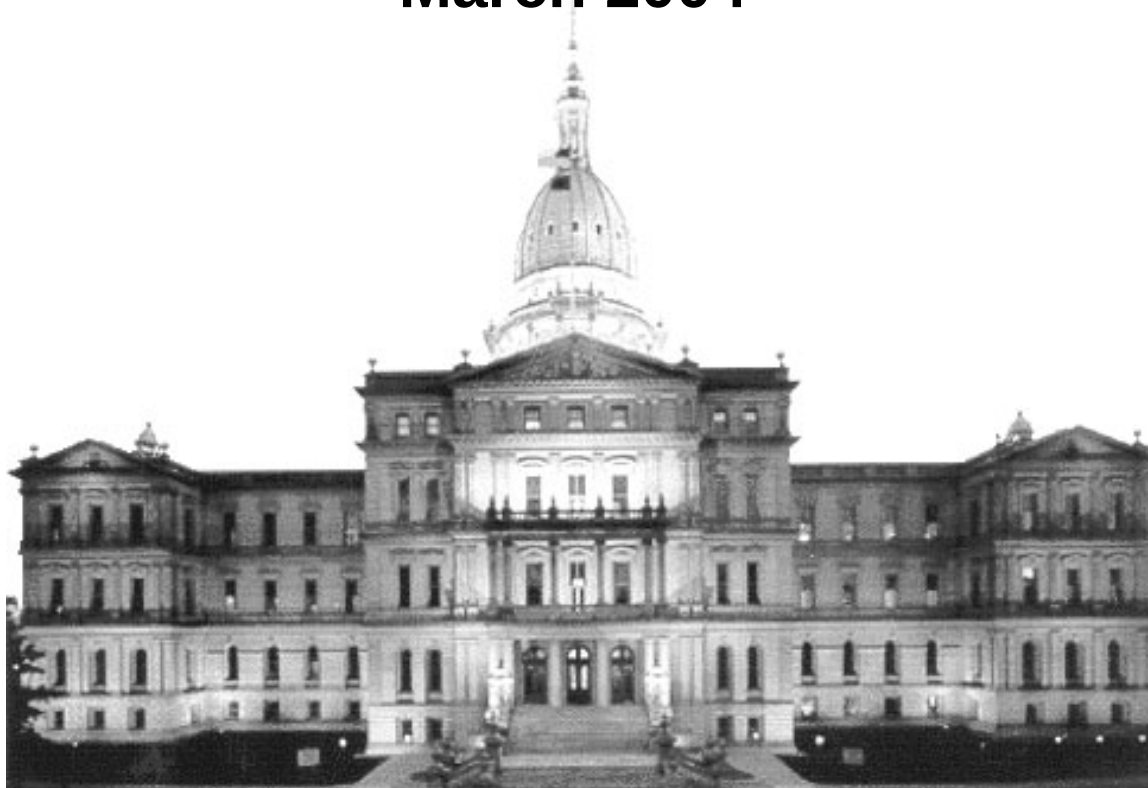




FY 2004-05
APPROPRIATIONS REPORT
Part I - Governor's Recommendations

March 2004



THE SENATE FISCAL AGENCY

The Senate Fiscal Agency is governed by a board of five members, including the majority and minority leaders of the Senate, the Chairperson of the Appropriations Committee of the Senate, and two other members of the Appropriations Committee of the Senate appointed by the Chairperson of the Appropriations Committee with the concurrence of the Majority Leader of the Senate, one from the minority party.

The purpose of the Agency, as defined by statute, is to be of service to the Senate Appropriations Committee and other members of the Senate. In accordance with this charge the Agency strives to achieve the following objectives:

1. To provide technical, analytical, and preparatory support for all appropriations bills.
2. To provide written analyses of all Senate bills, House bills and Administrative Rules considered by the Senate.
3. To review and evaluate proposed and existing State programs and services.
4. To provide economic and revenue analysis and forecasting.
5. To review and evaluate the impact of Federal budget decisions on the State.
6. To review and evaluate State issuance of long-term and short-term debt.
7. To review and evaluate the State's compliance with constitutional and statutory fiscal requirements.
8. To prepare special reports on fiscal issues as they arise and at the request of members of the Senate.

The Agency is located on the 8th floor of the Victor Office Center. The Agency is an equal opportunity employer.



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TABLE OF CONTENTS

Page

Summary of Major Changes for FY 2004-05

Table 1: FY 2004-05 Governor's Recommendation by Source of Funds	2
Figure A: Appropriations by Source of Funds FY 2004-05 Governor's Recommendation	3
Table 2: Adjusted Gross Appropriations FY 2003-04 Versus Governor's Recommendation	4
Figure B: Adjusted Gross FY 2004-05 Governor's Recommendation	5
Table 3: State Spending from State Resources FY 2003-04 Versus Governor's Recommendation.....	6
Figure C: State Spending from State Resources FY 2004-05 Governor's Recommendation	7
Table 4: General Fund/General Purpose FY 2003-04 Versus Governor's Recommendation.....	8
Figure D: General Fund/General Purpose FY 2004-05 Governor's Recommendation	9
Table 5: Governor's FY 2004-05 State Budget Proposed GF/GP Revenues Available to Support Appropriations.....	10
Table 6: Governor's FY 2004-05 Appropriation Recommendations Major Proposed Changes from FY 2003-04 Year-to-Date GF/GP Appropriations.....	11
Table 7: FY 2004-05 Governor's Recommendation GF/GP Funding Increases.....	12
Table 8: FY 2004-05 Governor's Recommendation GF/GP Funding Reductions	13
Table 9: FY 2004-05 Governor's Budget Recommendation Funding Shifts to Increase/(Reduce) GF/GP	15
Table 10: FY 2003-04 Supplemental Appropriations Included in Governor's FY 2004-05 Budget Message	17
Table 11: Actual and "Fully Funded" Revenue Sharing Payments Actual FY 2000-01 through Estimated FY 2004-05...	20
Table 12: Governor's FY 2004-05 Budget Recommendation State Employee Funding Increases	22
Table 13: FY 2004-05 Tobacco Settlement Appropriations.....	23
Table 14: Summary of Program Transfers.....	24
Table 15: State Payments to Local Units of Government Article IX, Section 30 Requirement.....	32
Table 16: Full-Time Equated Positions FY 2003-04 Versus Governor's Recommendation.....	33
Figure E: Full-Time Equated Positions FY 2004-05 Governor's Recommendation	34
Table 17: FY 2004-05 General Fund/General Purpose Revenues, Expenditures and Year-End Balance.....	35
Table 18: FY 2004-05 School Aid Fund Budget Revenues, Expenditures and Year-End Balance.....	36

Economic and Revenue Forecast

Table 19: Consensus Economic Forecast: 2004 and 2005.....	38
Table 20: Governor's Projected Total State Revenue FY 2003-04 and FY 2004-05	39
Table 21: General Fund/General Purpose Revenue Estimates FY 2003-04 and FY 2004-05.....	41
Table 22: School Aid Fund Revenue Estimates FY 2003-04 and FY 2004-05	42
Table 23: Governor's Proposed Tax Policy Changes FY 2004-05 Estimated Fiscal Impact by Fund	43

OVERVIEW

Governor Granholm on February 12, 2004, transmitted her fiscal year (FY) 2004-05 State Budget Message to the Legislature. The Governor's FY 2004-05 budget contains recommendations to provide for \$39.1 billion of Adjusted Gross appropriations. Included in this appropriations total are \$12.0 billion of Federal funds, \$17.4 billion of State Restricted funds, \$1.1 billion of local and private funds, and \$8.7 billion of General Fund/General Purpose (GF/GP) appropriations. Table 1 and Figure A provide summaries of the overall makeup of the FY 2004-05 appropriations recommended by the Governor.

Tables 2-4 and Figures B-D provide department-by-department detail of the Governor's appropriation requests for FY 2004-05 compared with FY 2003-04 year-to-date appropriations. The tables and figures present appropriation data in terms of Adjusted Gross, State Spending from State Resources, and GF/GP appropriations. Adjusted Gross appropriations are defined as total appropriations for each department less funds transferred in from other State departments. State Spending from State Resources appropriations are defined as Adjusted Gross appropriations less Federal and local and private funds. General Fund/General Purpose appropriations are the residual unrestricted portion of the budget over which the Governor and the Legislature have the most flexibility in establishing appropriation policy. The Governor's budget proposes a 1.7% increase in Adjusted Gross appropriations, a 1.7% increase in State Spending from State Resources appropriations, and a 2.4% decrease in GF/GP appropriations.

The Governor's Budget Message is developed based on the consensus revenue estimates agreed to on January 14, 2004. These consensus revenue estimates are the basis for the appropriation and tax policy changes contained in the Governor's budget recommendations. The FY 2004-05 GF/GP consensus revenue estimate represents a \$34.2 million or 0.4% decrease from the FY 2003-04 GF/GP consensus revenue estimate. The FY 2004-05 School Aid Fund consensus revenue estimate represents a \$414.2 million or 3.9% increase from the FY 2003-04 consensus revenue estimate. The Governor's budget also contains several recommended policy changes that will have an impact on the level of revenues available to support appropriations. These revenue adjustments include an increase in taxes for tobacco products, increases in the wholesale price of liquor, and the creation of a State specific estate tax. The consensus revenue estimates and the proposed tax policy changes will be discussed in more detail in the Economic and Revenue Forecast section of this report.

SUMMARY OF MAJOR CHANGES FOR FY 2004-05

The Governor's FY 2004-05 budget proposal marks the second State budget that Governor Granholm has transmitted to the Legislature. The Governor's budget contains revenue increases from proposed tax policy changes, revenue increases from proposed fee increases, appropriation increases to cover projected State expenditure needs, reductions in the funding of existing State programs, and proposed accounting changes that will affect the level of State appropriations.

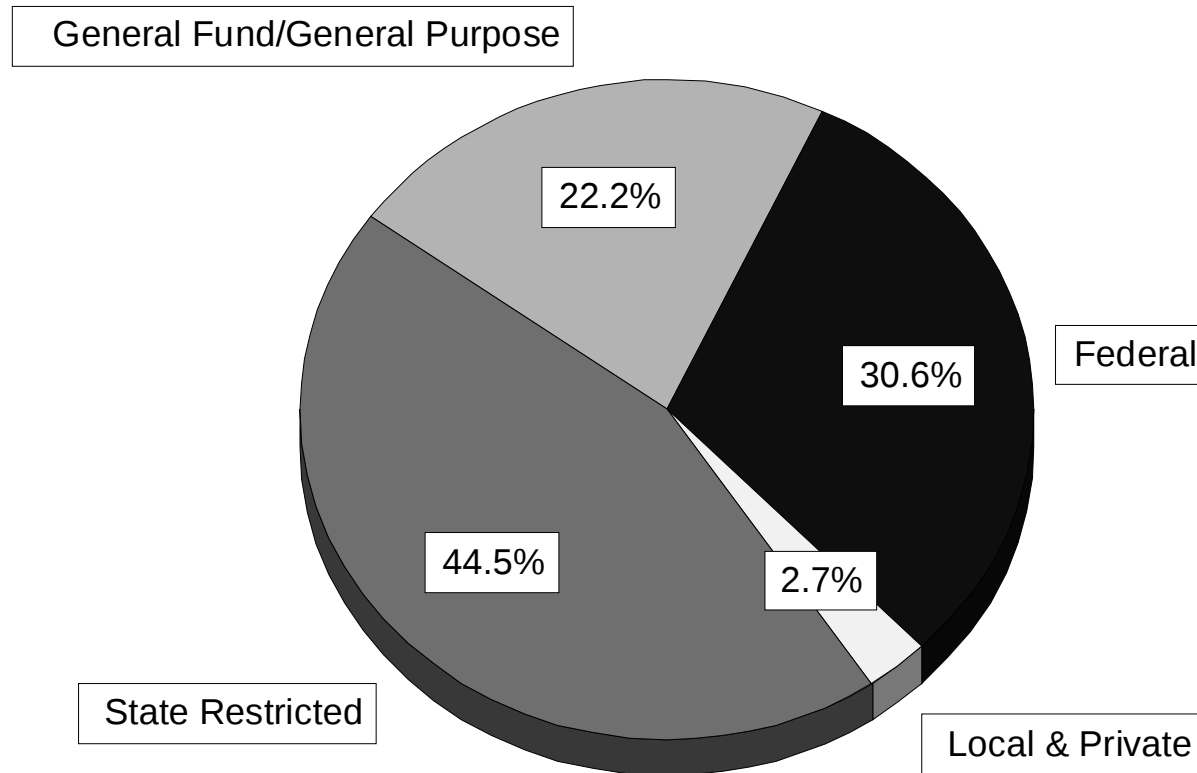
Table 1

**FY 2004-05 Governor's Recommendation
By Source of Funds
(actual dollars)**

Department/Budget Area	Adjusted Gross	Federal Funds	Local & Private Funds	State Restricted	General Funds
Agriculture	\$105,809,800	\$33,406,200	\$138,700	\$40,755,500	\$31,509,400
Attorney General	51,070,800	9,292,400	0	11,070,000	30,708,400
Capital Outlay	571,148,300	210,842,000	42,790,000	46,214,200	271,302,100
Civil Rights	12,791,200	934,000	0	0	11,857,200
Civil Service	32,962,900	4,779,100	1,850,000	18,545,500	7,788,300
Community Colleges	285,747,000	0	0	0	285,747,000
Community Health	9,732,387,800	4,987,951,800	894,992,300	1,373,364,900	2,476,078,800
Corrections	1,821,254,700	9,808,000	393,600	68,090,600	1,742,962,500
Education	114,481,300	60,654,600	5,900,200	19,472,200	28,454,300
Environmental Quality	326,345,000	133,766,800	445,900	153,980,000	38,152,300
Executive	4,859,500	0	0	0	4,859,500
Family Independence Agency	4,335,315,000	3,041,368,900	85,293,300	70,321,400	1,138,331,400
Higher Education	1,631,964,400	4,500,000	0	90,750,000	1,536,714,400
History, Arts, and Libraries	58,604,200	8,151,300	577,400	2,412,400	47,463,100
Information Technology	0	0	0	0	0
Judiciary	248,383,100	3,815,600	4,140,600	82,333,600	158,093,300
Labor and Economic Growth	1,218,761,400	792,629,400	19,461,000	297,760,900	108,910,100
Legislature	116,829,300	0	400,000	2,356,500	114,072,800
Management & Budget	70,762,300	444,600	0	33,206,100	37,111,600
Military Affairs	109,863,200	45,418,100	1,282,300	25,599,800	37,563,000
Natural Resources	250,372,400	34,629,300	2,024,300	188,075,700	25,643,100
School Aid	12,479,910,200	1,314,388,000	0	11,033,722,200	131,800,000
State	168,266,000	1,391,000	100	151,553,500	15,321,400
State Police	456,979,400	106,255,100	4,691,800	100,574,000	245,458,500
Transportation	3,292,487,600	1,132,701,200	5,800,000	2,153,986,400	0
Treasury (Debt Service)	81,450,400	0	0	10,887,300	70,563,100
Treasury (Operations)	354,761,800	34,681,800	964,300	262,095,700	57,020,000
Treasury (Revenue Sharing)	1,136,942,300	0	0	1,135,400,000	1,542,300
TOTAL APPROPRIATIONS	\$39,070,511,300	\$11,971,809,200	\$1,071,145,800	\$17,372,528,400	\$8,655,027,900

Figure A

Appropriations by Source of Funds FY 2004-05 Governor's Recommendation



Total = \$ 39,070,511,300

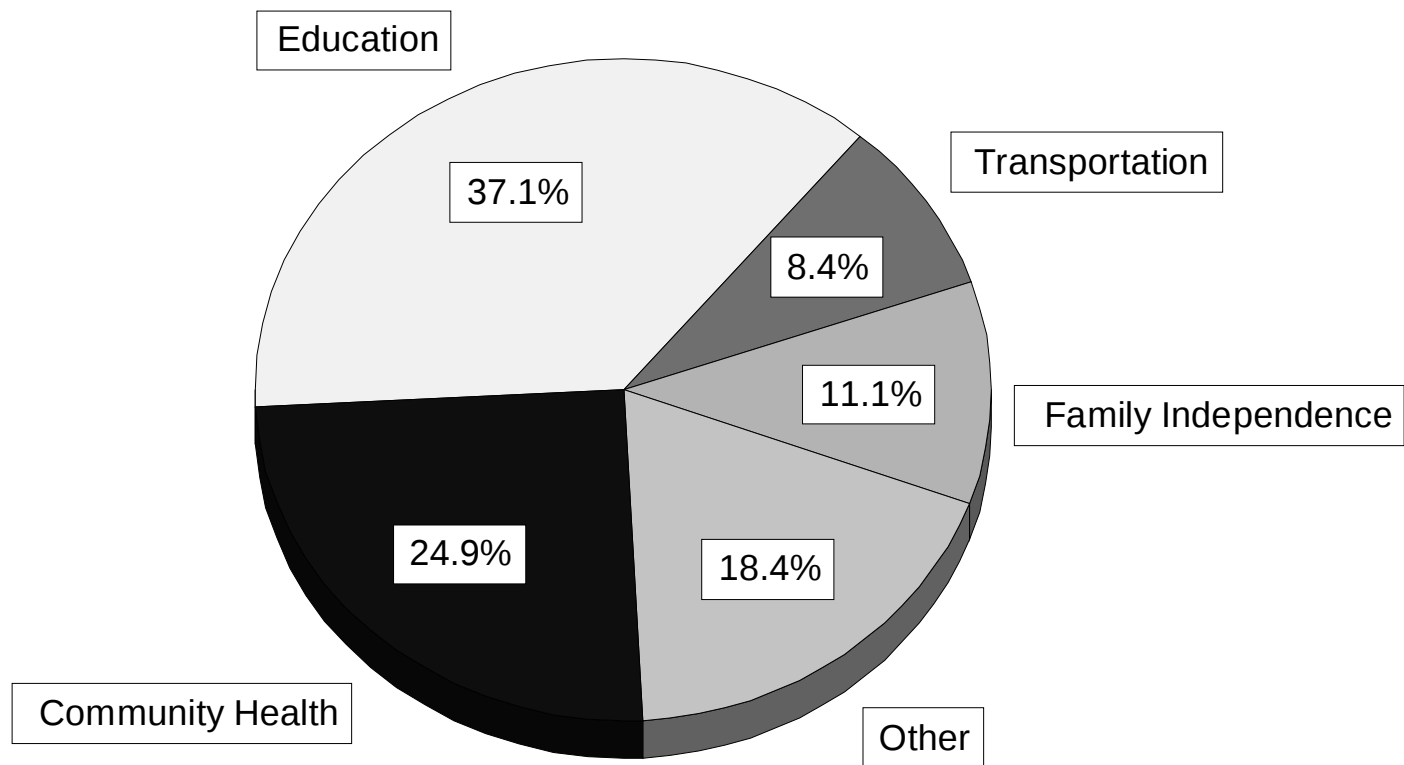
Table 2

**Adjusted Gross Appropriations
FY 2003-04 Versus Governor's Recommendation
(actual dollars)**

Department/Budget Area	FY 2003-04 Year-to-Date Appropriations	FY 2004-05 Governor's Recommendation	Dollar Difference	Percent Change
Agriculture	\$85,720,400	\$105,809,800	\$20,089,400	23.4%
Attorney General	49,929,800	51,070,800	1,141,000	2.3
Capital Outlay	560,464,100	571,148,300	10,684,200	1.9
Career Development	461,595,374	0	(461,595,374)	(100.0)
Civil Rights	12,654,158	12,791,200	137,042	1.1
Civil Service	29,333,837	32,962,900	3,629,063	12.4
Community Colleges	285,096,800	285,747,000	650,200	0.2
Community Health	9,643,401,300	9,732,387,800	88,986,500	0.9
Consumer and Industry Services	604,530,718	0	(604,530,718)	(100.0)
Corrections	1,702,518,881	1,821,254,700	118,735,819	7.0
Education	107,281,200	114,481,300	7,200,100	6.7
Environmental Quality	357,264,475	326,345,000	(30,919,475)	(8.7)
Executive	4,859,500	4,859,500	0	0.0
Family Independence Agency	3,952,345,500	4,335,315,000	382,969,500	9.7
Higher Education	1,697,566,200	1,631,964,400	(65,601,800)	(3.9)
History, Arts, and Libraries	56,410,500	58,604,200	2,193,700	3.9
Judiciary	248,434,400	248,383,100	(51,300)	(0.0)
Labor and Economic Growth	0	1,218,761,400	1,218,761,400	0.0
Legislature	116,967,900	116,829,300	(138,600)	(0.1)
Management & Budget	67,771,000	70,762,300	2,991,300	4.4
Military Affairs	102,797,500	109,863,200	7,065,700	6.9
Natural Resources	250,026,100	250,372,400	346,300	0.1
School Aid	12,475,669,000	12,479,910,200	4,241,200	0.0
State	161,088,251	168,266,000	7,177,749	4.5
State Police	436,237,529	456,979,400	20,741,871	4.8
Strategic Fund Agency	102,236,509	0	(102,236,509)	(100.0)
Transportation	3,107,818,700	3,292,487,600	184,668,900	5.9
Treasury (Debt Service)	56,286,400	81,450,400	25,164,000	44.7
Treasury (Operations)	369,022,586	354,761,800	(14,260,786)	(3.9)
Treasury (Revenue Sharing)	1,316,866,500	1,136,942,300	(179,924,200)	(13.7)
TOTAL APPROPRIATIONS	\$38,422,195,118	\$39,070,511,300	\$648,316,182	1.7%

Figure B

Adjusted Gross FY 2004-05 Governor's Recommendation



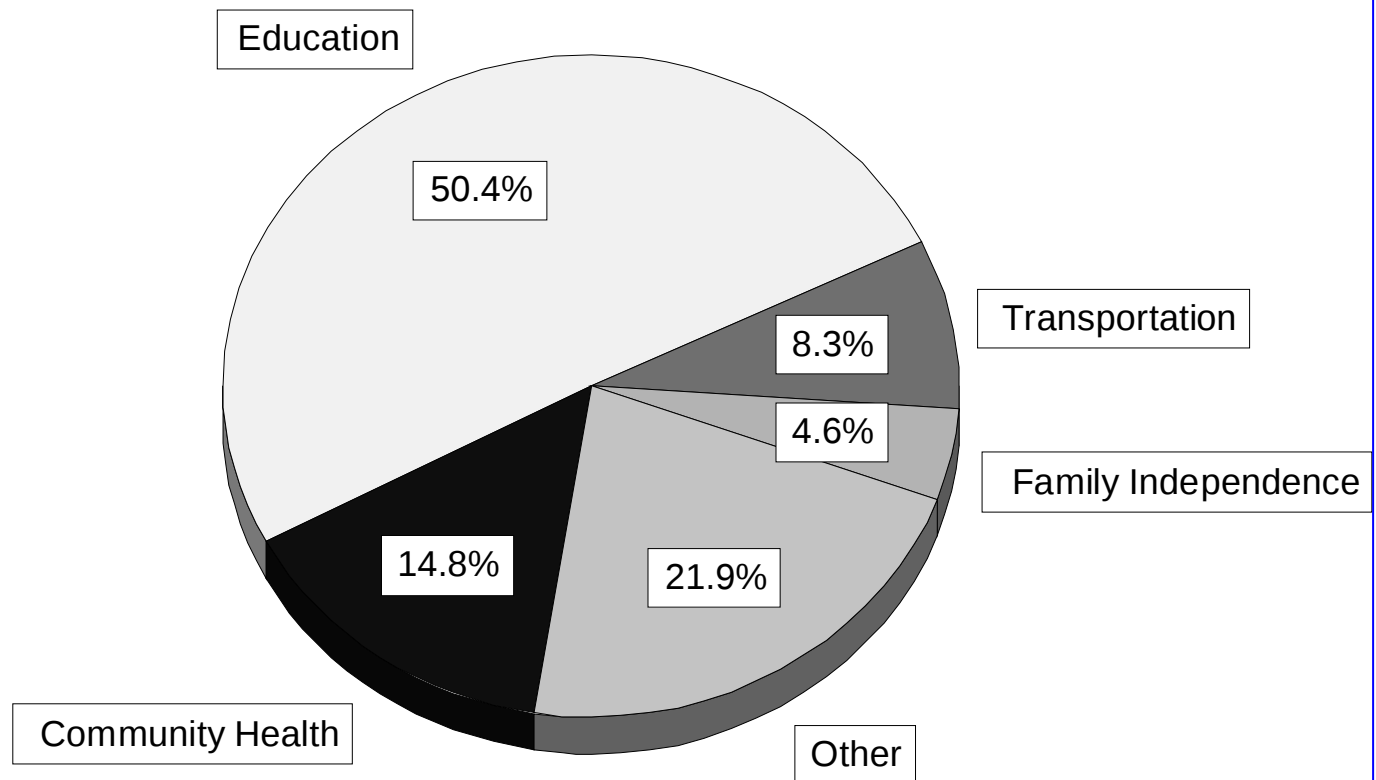
Total = \$ 39,070,511,300

Table 3
State Spending from State Resources
FY 2003-04 Versus Governor's Recommendation
(actual dollars)

Department/Budget Area	FY 2003-04 Year-to-Date Appropriations	FY 2004-05 Governor's Recommendation	Dollar Difference	Percent Change
Agriculture	\$70,191,100	\$72,264,900	\$2,073,800	3.0%
Attorney General	40,930,000	41,778,400	848,400	2.1
Capital Outlay	310,722,500	317,516,300	6,793,800	2.2
Career Development	29,999,674	0	(29,999,674)	(100.0)
Civil Rights	11,720,158	11,857,200	137,042	1.2
Civil Service	22,704,737	26,333,800	3,629,063	16.0
Community Colleges	285,096,800	285,747,000	650,200	0.2
Community Health	3,391,092,600	3,849,443,700	458,351,100	13.5
Consumer and Industry Services	318,109,218	0	(318,109,218)	(100.0)
Corrections	1,674,329,381	1,811,053,100	136,723,719	8.2
Education	35,911,300	47,926,500	12,015,200	33.5
Environmental Quality	225,569,275	192,132,300	(33,436,975)	(14.8)
Executive	4,859,500	4,859,500	0	0.0
Family Independence Agency	1,171,075,800	1,208,652,800	37,577,000	3.2
Higher Education	1,693,085,500	1,627,464,400	(65,621,100)	(3.9)
History, Arts, and Libraries	46,510,500	49,875,500	3,365,000	7.2
Judiciary	240,336,700	240,426,900	90,200	0.0
Labor and Economic Growth	0	406,671,000	406,671,000	0.0
Legislature	116,567,900	116,429,300	(138,600)	(0.1)
Management & Budget	67,030,200	70,317,700	3,287,500	4.9
Military Affairs	60,898,900	63,162,800	2,263,900	3.7
Natural Resources	214,448,100	213,718,800	(729,300)	(0.3)
School Aid	11,158,987,100	11,165,522,200	6,535,100	0.1
State	159,768,651	166,874,900	7,106,249	4.4
State Police	327,828,629	346,032,500	18,203,871	5.6
Strategic Fund Agency	48,430,109	0	(48,430,109)	(100.0)
Transportation	2,160,263,600	2,153,986,400	(6,277,200)	(0.3)
Treasury (Debt Service)	56,286,400	81,450,400	25,164,000	44.7
Treasury (Operations)	323,415,686	319,115,700	(4,299,986)	(1.3)
Treasury (Revenue Sharing)	1,316,866,500	1,136,942,300	(179,924,200)	(13.7)
TOTAL APPROPRIATIONS	\$25,583,036,518	\$26,027,556,300	\$444,519,782	1.7%

Figure C

State Spending from State Resources FY 2004-05 Governor's Recommendation



Total = \$ 26,027,556,300

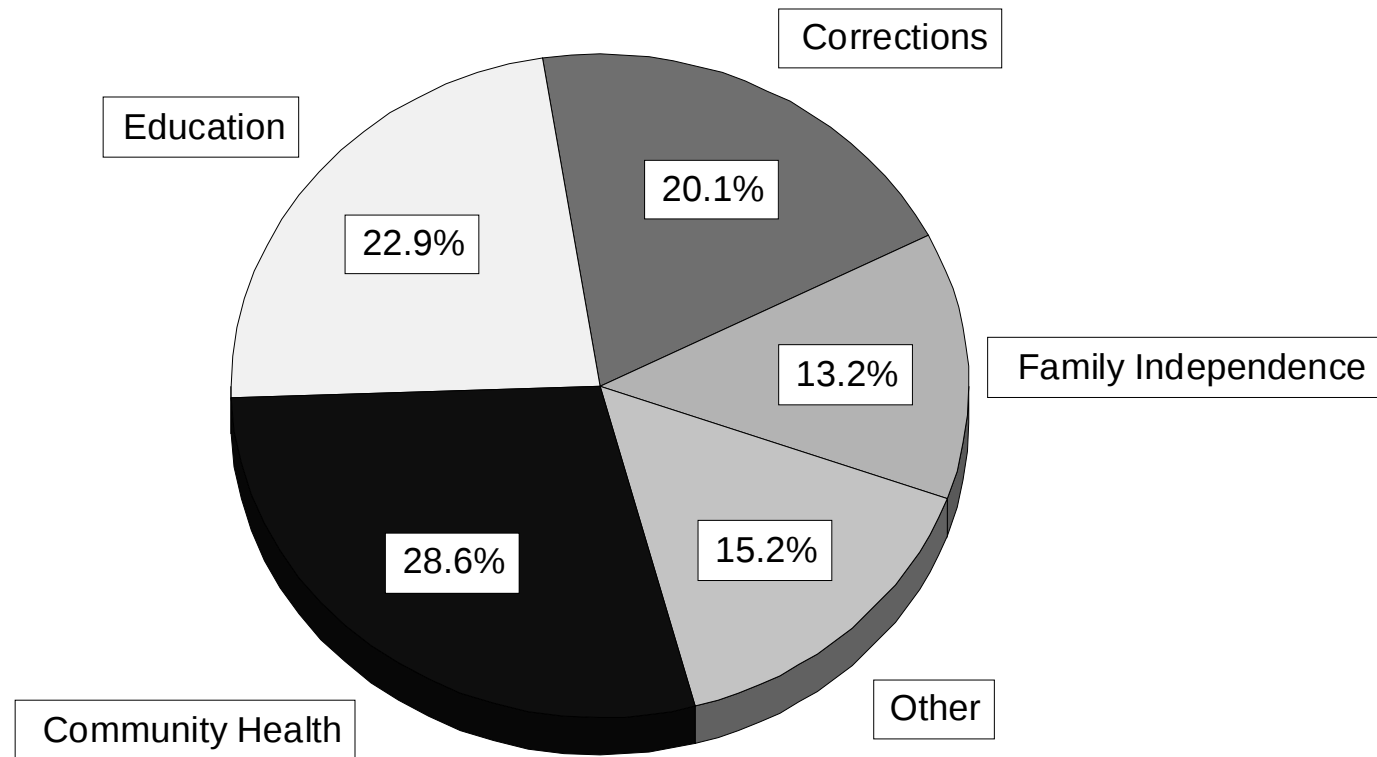
Table 4

**General Fund/General Purpose
FY 2003-04 Versus Governor's Recommendation**

Department/Budget Area	FY 2003-04 Year-to-Date Appropriations	FY 2004-05 Governor's Recommendation	Dollar Difference	Percent Change
Agriculture	\$30,259,200	\$31,509,400	\$1,250,200	4.1%
Attorney General	30,259,900	30,708,400	448,500	1.5
Capital Outlay	252,302,500	271,302,100	18,999,600	7.5
Career Development	24,334,974	0	(24,334,974)	(100.0)
Civil Rights	11,720,158	11,857,200	137,042	1.2
Civil Service	7,832,537	7,788,300	(44,237)	(0.6)
Community Colleges	285,096,800	285,747,000	650,200	0.2
Community Health	2,652,980,300	2,476,078,800	(176,901,500)	(6.7)
Consumer and Industry Services	15,965,418	0	(15,965,418)	(100.0)
Corrections	1,609,272,281	1,742,962,500	133,690,219	8.3
Education	29,059,700	28,454,300	(605,400)	(2.1)
Environmental Quality	53,580,775	38,152,300	(15,428,475)	(28.8)
Executive	4,859,500	4,859,500	0	0.0
Family Independence Agency	1,100,979,000	1,138,331,400	37,352,400	3.4
Higher Education	1,603,335,500	1,536,714,400	(66,621,100)	(4.2)
History, Arts and Libraries	44,201,700	47,463,100	3,261,400	7.4
Judiciary	160,216,400	158,093,300	(2,123,100)	(1.3)
Labor and Economic Growth	0	108,910,100	108,910,100	0.0
Legislature	114,072,800	114,072,800	0	0.0
Management & Budget (Operations)	35,828,900	37,111,600	1,282,700	3.6
Military Affairs	36,328,800	37,563,000	1,234,200	3.4
Natural Resources (Operations)	28,089,400	25,643,100	(2,446,300)	(8.7)
School Aid	327,700,000	131,800,000	(195,900,000)	(59.8)
State	16,698,451	15,321,400	(1,377,051)	(8.2)
State Police	234,765,229	245,458,500	10,693,271	4.6
Strategic Fund Agency	38,380,109	0	(38,380,109)	(100.0)
Transportation	0	0	0	0.0
Treasury (Debt Service)	55,408,400	70,563,100	15,154,700	27.4
Treasury (Operations)	60,263,986	57,020,000	(3,243,986)	(5.4)
Treasury (Revenue Sharing)	1,542,300	1,542,300	0	0.0
TOTAL APPROPRIATIONS	\$8,865,335,018	\$8,655,027,900	(\$210,307,118)	(2.4)%

Figure D

General Fund/General Purpose FY 2004-05 Governor's Recommendation



Total = \$ 8,655,027,900

As previously stated, the Governor's FY 2004-05 budget recommendation is built on assumptions as to the level of revenues available to support appropriations. Table 5 provides a summary of the amount of total GF/GP revenue that will be available to support FY 2004-05 GF/GP appropriations. Total FY 2004-05 GF/GP revenue assumed in the Governor's budget equals \$8.66 billion. This revenue total includes \$7.82 billion of consensus revenues and \$246.6 million of enacted revenue adjustments not included in the consensus revenue estimate. These enacted revenue adjustments include fee increases, revenue generated from the enhanced enforcement of State tax laws, and changes in laws governing the escheating of property. The Governor's budget includes \$590.7 million of other revenue adjustments that will have an impact on GF/GP revenue. These include an increase in the wholesale price of liquor, a freeze in the level of revenue sharing payments to cities, villages, townships and counties, the proposed suspension of statutory revenue sharing payments to counties offset by an acceleration of county property tax collections, and changes in the estimated costs to the General Fund for borrowing funds from other State funds.

Table 5 Governor's FY 2004-05 State Budget Proposed General Fund/General Purpose Revenues Available to Support Appropriations (millions of dollars)	
	Governor's Recommendation
Revenues:	
Consensus Revenue Estimate	\$7,822.8
Enacted Revenue Adjustments:	
Enhanced Tax Enforcement Revenue	85.1
Driver Responsibility Legislation.....	121.5
Driver License Fee Legislation	25.0
Escheats Law Change	15.0
Subtotal Enacted Revenue Adjustments	\$246.6
Subtotal Current Law Revenue	\$8,069.4
Proposed Revenue Adjustments:	
Increase Liquor Markup to 74%	31.8
Freeze Revenue Sharing	355.4
Suspend County Revenue Sharing Payments.....	183.5
Adjust Interfund Borrowing Costs.....	20.0
Subtotal Proposed Revenue Adjustments	\$590.7
Total Estimated Revenue.....	\$8,660.1

Table 6 provides a comparison of the Governor's recommended level of FY 2004-05 GF/GP appropriations with the year-to-date level of FY 2003-04 GF/GP appropriations. The Governor's recommendation represents a \$210.3 million or 2.4% decline in GF/GP appropriations. Table 6 provides a high-level summary of the three approaches recommended by the Governor to deal with this \$210.3 million reduction in FY 2004-05 GF/GP appropriations. The \$210.3 million of appropriation reductions is made up of \$521.2 million of GF/GP appropriation increases, \$436.3 million of GF/GP appropriation reductions, and \$295.2 million of appropriation reductions and increases that offset changes in Federal or State Restricted funding, but do not have an impact on the overall level of State programs.

Table 6 Governor's FY 2004-05 Appropriation Recommendations Major Proposed Changes from FY 2003-04 Year-to-Date General Fund/General Purpose Appropriations (millions of dollars)	
FY 2003-04 Year-to-Date Appropriations	\$8,865.3
FY 2004-05 Governor's Appropriation Recommendations	<u>8,655.0</u>
Net Decrease in Appropriations	\$ (210.3)
<u>Major FY 2004-05 Appropriation Recommendations:</u>	
Proposed Funding Increases	\$ 521.2
Proposed Appropriation Reductions	(436.3)
Fee Increases/Fund Shifts	<u>(295.2)</u>
Total	\$ (210.3)

Table 7 provides a summary of the \$521.2 million of GF/GP appropriation increases recommended in the FY 2004-05 budget. These appropriation increases can be grouped into three categories. First are increases dealing with caseload and general cost adjustments. These include funding increases in the Department of Community Health for Medicaid and other programs, in the Department of Corrections for prison operating costs, and in the Family Independence Agency for caseload and general costs. The second general category of cost increases is debt service-related costs. These increases involve debt service costs on State Building Authority bonds in the Capital Outlay budget and general obligation bond debt service increases in the Department of Treasury budget. The final category of appropriation increases involves numerous other funding issues, the largest being the cost increases built into departmental budgets to fund projected State employee wages and salaries and the associated fringe benefits.

Table 7

FY 2004-05 Governor's Recommendation GF/GP Funding Increases (millions of dollars)	
<u>Department/Program</u>	
Capital Outlay	
State Building Authority Debt Service Payments.....	\$ 19.0
Community Colleges	
Renaissance Zone Reimbursement	0.7
Community Health	
Medicaid Caseload, Utilization and Inflation	100.1
Medicaid HMO Actuarial Base Funding.....	53.7
Community Mental Health Actuarial Base Funding	12.7
Adult Benefit Waiver Caseload	9.7
Corrections	
Funding for 1,000 Additional Beds.....	13.9
Salary Step Increases Due to Seniority.....	12.1
Hepatitis C Testing and Treatment.....	5.6
Parole/Community Placement	3.9
Training and Training Facility Rent.....	1.6
Pharmaceutical Cost Increases	1.2
Various Other Funding Increases	6.1
Family Independence Agency	
Caseload Increases	15.3
History, Arts, and Libraries	
Preservation and Access Project.....	1.5
Military and Veterans Affairs	
Retiree Payments	0.2
Challenge Program	0.1
State	
Qualified Voter File	0.4
State Police	
DNA Profiling Backlog.....	1.0
Treasury-Debt Service	
Quality of Life Bond Debt Service.....	22.2
Clean Michigan Initiative Bond Debt Service.....	3.1
Statewide Employee Economic Adjustments	237.1
Total Funding Increases	\$521.2

Table 8 provides a summary of the \$436.3 million of GF/GP appropriation reductions recommended in the FY 2004-05 budget. The major reduction is a \$195.9 million reduction in the level of the GF/GP grant to the School Aid Fund. Other major appropriation reductions include the elimination of the Tuition Grant Program in the Higher Education budget and proposed reductions in State employee compensation costs that will be achieved by negotiated reductions agreed to by the Office of the State Employer and State employee unions.

Table 8 FY 2004-05 Governor's Recommendation GF/GP Funding Reductions (millions of dollars)	
<u>Department/Program</u>	
Agriculture	
Marketing Program Elimination	\$ (0.2)
Civil Service	
Reductions in Contracts, Travel and HRNM System	(0.6)
Community Health	
Pharmaceutical Savings	(16.0)
Long-Term Care Policy Changes	(10.7)
Medicaid Third Party Liability for Noncustodial Parents	(6.5)
Elimination of Managed Care from Children's Special Health Care	(3.1)
Medicaid Notification of Injury Lawsuit Settlements	(2.0)
Medicaid Emergency Room Reimbursement Rates	(3.0)
Medicaid Incontinent Supply Vendor	(1.0)
Corrections	
Western Wayne Closure and Huron Valley Transfer	(20.5)
Security Technology Enhancements to Reduce Staff	(12.8)
Education	
School Breakfast Program	(0.3)
Family Independence Agency	
Child Support Enforcement System	(2.8)
Maxey Training Center Unit Closure	(0.6)
Wayne County Foster Care Permanency Project	(1.2)
Various Other Reductions	(3.0)
Higher Education	
Michigan State University-Agricultural Experiment Station	(1.0)
Michigan State University-Cooperative Extension Service	(0.9)
Tuition Grant Program	(64.8)

Table 8 (continued) FY 2004-05 Governor's Recommendation GF/GP Funding Reductions (millions of dollars)	
Judiciary	
Court Equity Funding	(1.0)
Elimination of Existing Judgeships	(0.1)
Management and Budget	
MAIN Contract Revisions	(0.5)
Military and Veterans Affairs	
Elimination of One-Time Guard Travel for Holidays	(0.1)
School Aid Fund	
Reduction of GF/GP Grant	(195.9)
State Police	
Consolidation of Regional Dispatch Centers.....	(0.4)
Treasury-Operations	
Qualified Agricultural Loans Repayments	(3.0)
Enhanced Tax Enforcement.....	(0.6)
Information Technology Reductions.....	(0.8)
Statewide Employee Concessions	(76.2)
Statewide Information Technology Programs.....	(4.5)
Human Resources Optimization	(2.2)
Total	\$(436.3)

Table 9 provides a summary of the funding shifts that are included in the GF/GP budget recommendation. These funding shifts do not increase or decrease the overall level of any specific State program, but simply substitute GF/GP appropriations to offset the loss of Federal or State Restricted funds or reduce GF/GP funding to offset increases in Federal or State Restricted funds. The primary department affected by these funding shifts is the Department of Community Health, in which numerous changes are made to replace Federal or State Restricted funds with GF/GP appropriations. The net effect of these fund shifts is a \$295.2 million reduction in GF/GP appropriations.

Table 9

FY 2004-05 Governor's Budget Recommendation Funding Shifts to Increase/(Reduce) GF/GP (millions of dollars)	
<u>Department/Program</u>	
Community Health	
Vital Records Fee Increase	\$ (1.5)
Tobacco Tax Revenue to Offset GF/GP Medicaid	(419.1)
Tobacco Settlement Revenue Fund Shifts	(68.2)
Estate Tax Revenue to Offset GF/GP Medicaid	(94.3)
Replacing One-Time Federal Medicaid Funds with GF/GP	168.4
Increase in Federal Medicaid Match Rate to Reduce GF/GP	(65.8)
Replacing Medicaid Federal Special Financing with GF/GP	152.6
Mental Health Quality Assessment Program	(3.5)
Pharmacy Quality Assessment Shift to GF/GP	18.9
HMO Quality Assessment Adjustments	(18.5)
Corrections	
Parole/Probation Fees to Offset GF/GP	(0.5)
Resident Stores Revenue Increase	(0.3)
Annualizing Public Works Fee Increase	(0.1)
Youth Prison Replacing Federal with GF/GP	18.0
Education	
Teacher Certification Fee Fund Shift	(0.6)
Environmental Quality	
Water Pollution Revolving Loan Program Shift to Restricted	(16.3)
Family Independence Agency	
Replacing One-Time Federal Penalty Funds with GF/GP	14.1
History, Arts and Libraries	
Replacing Federal for Detroit/Grand Rapids Libraries with GF/GP	1.1
Judiciary	
Increase in Drug Court Fund Revenue	(0.4)
Increase in Court Equity Fund Revenue	(1.8)
Labor and Economic Growth	
Work First Program Replacing Federal with GF/GP	39.9
Fire Marshal Replacing GF/GP with Restricted	(1.6)

Table 9 (continued)

FY 2004-05 Governor's Budget Recommendation Funding Shifts to Increase/(Reduce) GF/GP (millions of dollars)	
Management and Budget	
Mail Service Funding Shift.....	(0.2)
Natural Resources	
Purchased Lands Tax Payments Shift to Restricted.....	(2.0)
Forest Fire Protection Shift to Restricted.....	(1.0)
State	
Mainframe Computer from GF/GP to Restricted.....	(1.0)
State Police	
At-Post Trooper Replacement with Restricted.....	(1.5)
Treasury-Debt Service	
Quality of Life Bonds Replacement with Restricted	(10.0)
Total	\$(295.2)

FY 2003-04 Supplemental Appropriations. The Governor's FY 2004-05 budget message contains a series of recommended FY 2003-04 supplemental appropriations. Table 10 provides a summary of these recommended supplemental appropriations. The supplemental appropriations total \$231.8 million of Gross appropriations and zero of GF/GP appropriations. These supplemental appropriations provide for the appropriation of additional Federal and State Restricted funds received by the State and not yet appropriated in FY 2003-04.

Table 10

FY 2003-04 Supplemental Appropriations Included in Governor's FY 2004-05 Budget Message (actual dollars)		
Department/Program	Gross Appropriation	GF/GP Appropriation
Agriculture		
Emerald Ash Borer Eradication	\$17,750,000	\$ 0
Attorney General		
Medicaid Fraud Programs	433,934	0
Community Health		
Departmentwide Administration.....	654,800	0
Mental Health/Substance Abuse Grants	2,133,000	0
State Mental Health Facilities	17,841,000	0
Public Health Administration.....	370,300	0
Laboratory Services.....	1,991,500	0
Epidemiology	1,195,700	0
Local Health Administration	100,000	0
Chronic Disease and Injury Prevention	4,322,900	0
Community Living, Children and Families	911,700	0
Office of Services to the Aging	670,000	0
Medical Service Administration	3,000,000	0
Medical Services.....	11,112,600	0
Information Technology	8,800,000	0
Education		
Professional Preparation Services	150,000	0
Environmental Quality		
Electronic Reporting System	275,000	0
Family Independence Agency		
Family Independence Program	26,056,100	0
Day Care Services.....	17,809,300	0
Food Assistance Benefits	102,444,200	0
Information Technology		
Administration	8,800,000	0
Natural Resources		
Snowmobile Trail Development Grants	4,000,000	0
Retail License System	350,000	0
State		
Notary Law Changes	190,000	0
Election Regulation.....	410,000	0
Total.....	\$231,772,034	\$ 0

Proposed State Tax Policy and Revenue Changes. The budget recommendation includes numerous proposals to increase State revenues that will be contingent on legislative approval of a variety of statutory amendments. These changes include \$295.0 million of new revenue from an increase in the excise taxes on tobacco products, \$94.0 million from the imposition of a State estate tax, and \$35.5 million from an increase in the wholesale price of liquor. These proposed tax policy changes are discussed in detail in the Economic and Revenue Forecast portion of this report.

Federal Funds Assumptions. The recommended appropriation of \$11.97 billion of Federal funds in the overall State budget is based on Federal budget policy currently in place. The FY 2005 Federal budget is not likely to pass before October 1, 2004, and the Federal funding assumptions used in the State budget will assume that the level of Federal funds authorized to Michigan in FY 2004-05 will be equal to the level of Federal funds received in FY 2003-04. The only exceptions to this assumption will be the elimination of Federal funds that is already known due to previously enacted changes in Federal policy or the elimination of one-time sources of Federal funding in the State budget.

State Revenue Sharing. The Governor's FY 2004-05 budget contains several recommended changes to the level of State revenue sharing payments to cities, villages, townships, and counties. Table 11 provides a history of State Revenue Sharing appropriations for the period FY 2000-01 through the FY 2004-05 recommendation. These changes include:

Advancement of Collection Date for County Property Taxes. In order to offset the impact of reducing revenue sharing payments to counties, the Governor's budget recommendation for FY 2004-05 recommends that the date county property taxes are levied be permanently accelerated from December of each year to July.

- In the initial year of the acceleration, a \$1.4 billion one-time increase in county property taxes would occur in FY 2003-04. The accelerated collection would be placed in a restricted revenue fund subject to separate reporting requirements and statutory restrictions on withdrawals.
- Withdrawals in future years would be adjusted for inflation and as the fund was depleted, statutory revenue sharing payments would begin again -- sometime between approximately FY 2008-09 and FY 2026-27.
- Apparently local units could borrow against the full amount to meet cash flow needs. However, on an annual basis, not more than the allowed amount could be permanently withdrawn from the fund.
- No restrictions are placed on the timing of withdrawals or the amounts that could be withdrawn, other than on the total amount that could be permanently withdrawn during a year. A local unit essentially could receive the equivalent of a full year of revenue sharing payments on the first day of the fiscal year.

Replacement of Payments in lieu of Taxes (PILT) for State-Owned Land. For certain State-owned land, the State has historically made ad valorem payments to the local units in which the land is located to offset the reduction in property taxes that occurred when the State assumed ownership of the land. The Governor's FY 2004-05 budget proposes using an estimated \$7.5 million to fund

permanently the payments to local units with statutory revenue sharing funds that otherwise would be distributed to all cities, villages, and townships (CVTs).

- Payments to replace PILT would be the first obligation funded with statutory revenue sharing funds. After PILT replacements were funded, the remaining portion of the statutory appropriation would be distributed according to the formula or any other provisions contained in statute.
- Taxable values used to compute payments would be fixed at the 2003 valuations and additional property the State acquires would be valued when added.
- The millage rates used to compute payments would exclude special assessments, the State education tax, and any increase in other property tax millage rates above those levied in 2003.
- The aggregate amount available for PILT would grow at the same rate as the total of combined constitutional and statutory revenue sharing payments received by cities, villages, and townships. Within that aggregate amount, payments would be prorated.
- No payments would be made to any jurisdiction where the PILT would be less than \$500 during a fiscal year.

Reduction in Statutory Revenue Sharing Payments. The Governor's budget recommendation for FY 2004-05 revenue sharing payments totals \$1.135 billion, a 15% decrease from the current appropriation and a 13.7% reduction from the payments forecasted based upon the January 2004 consensus revenue estimates.

- Approximately \$183.5 million of the \$200.4 million reduction reflects proposed reductions in the payments to counties, while virtually all of the remainder reflects that actual FY 2003-04 payments will be below the appropriation.
- Of the portion distributed to cities, villages and townships, the administration estimates that \$7.5 million would be used to fund PILT reimbursements. Combined with the recommendation for statutory revenue sharing payments of \$443.5 million, non-PILT-related statutory revenue sharing payments to CVTs would be 99.3% of the payment received in FY 2003-04.
- Not all local units would receive a payment that was 99.3% of the FY 2003-04 payment. Approximately 240 local units would receive a 4.3% increase because they are estimated to cease receiving statutory revenue sharing payments during FY 2003-04. As a result, their total payment, excluding PILT replacement payments, would grow at the same rate as sales tax revenue, currently estimated at 4.3%.
- Under the administration's estimates, approximately 740 local units no longer would receive a statutory revenue sharing payment. Excluding PILT replacement payments, combined constitutional and statutory revenue sharing payments to approximately 500 of these local units that lose their statutory revenue sharing payments in FY 2004-05 would be between 99.3% and 104.3% of their FY 2003-04 payment.

Combined with the changes in county payments and the PILT replacement, statutory revenue sharing payments would be \$538.9 million below the "fully-funded" level.

Hold-Harmless Grants to Units with Emergency Financial Managers. In FY 2003-04, local units under the control of a State-appointed emergency financial manager (Flint, Hamtramck, Highland Park) received \$1.5 million in grants to hold them harmless from the revenue sharing reductions in Executive Order 2003-23. The Governor's budget recommends again providing \$1.5 million in hold-harmless grants. The grants would be funded by the General Fund rather than restricted sales tax revenue.

Table 11

Actual and "Fully Funded" Revenue Sharing Payments Actual FY 2000-01 through Estimated FY 2004-05 (dollars in millions)					
Fiscal Year	Estimated Fully Funded	Percent Change	Actual Payments	Percent Change	Effective Reductions
2000-01	\$1,555.5	2.3%	\$1,555.5	6.4%	\$ 0.0
2001-02	1,571.3	1.0%	1,517.3	(2.5)%	(54.0)
2002-03	1,597.9	1.7%	1,451.4	(4.3)%	(146.5)
Est. 2003-04 ^{a)}	1,605.0	0.4%	1,315.3	(9.4)%	(289.7)
Est. 2004-05 ^{b)}	1,674.3	4.3%	1,127.9	(14.2)%	(546.4)
a) FY 2003-04 and FY 2004-05 estimates are based upon the January 2004 consensus revenue estimates, adjusted for Executive Order 2003-23 and Public Act 237 of 2003 (House Bill 4367). Actual payments will differ from the estimates presented depending on how actual revenues differ from the January 2004 estimates.					
b) FY 2004-05 estimates exclude \$7.5 million in payments in lieu of taxes (PILT) to selected local units, as well as \$1.5 million in hold harmless grants funded from the General Fund to units with State-appointed emergency financial managers.					

General Budget Language. The budget includes several recommendations concerning standard budget language. The budget eliminates the past practice of freezing classified State employment levels unless exceptions are granted by the State Budget Director. The recommendation also includes language to provide for appropriations of unanticipated Federal, State Restricted, or local and private funds through the contingency fund transfer process. This type of appropriation transfer was eliminated in the enacted FY 2003-04 appropriation bills.

Proposed Fee Increases. The budget recommendation contains two proposed increases in State fees. The vital records fee levied by the Department of Community Health would be increased to generate \$1.5 million of increased State Restricted revenue. This revenue would be used to offset existing appropriations financed with GF/GP funding. The fee for the certification of assessors

charged by the Department of Treasury would be increased to generate \$80,000. This fee revenue would support existing programs involving assessors.

Unclassified Salaries. The budget includes no funding increases for unclassified salaries above the amounts appropriated in the current fiscal year.

State Classified Employee Funding Increases. The Governor's budget recommendation includes additional funding for State departments to provide for the previously negotiated pay increases and the associated fringe benefit cost increases for State employees. During FY 2003-04 the enacted State budget did not include funding for State employee cost increases. These cost increases were offset by a variety of concessions agreed to by the State employee unions and the Office of the State Employer. The FY 2004-05 budget recommendation includes funding for FY 2004-05 wage increases, insurance cost increases, retirement contribution cost increases, workers' compensation costs, and the building occupancy costs for the office spaces occupied by State employees. State employees are scheduled to receive a 4.0% increase in their salaries on October 1, 2004. This salary increase also affects the amount of funds the State must contribute to the Defined Benefit and Defined Contribution retirement systems to which all State employees belong.

The budget recommendation does assume that State employees will give up a portion of their wage increases through concessions that will be negotiated by the Office of the State Employer and the State employee unions. Table 12 provides a summary of the costs built into the Governor's budget for State employee salary and benefit increases.

Table 12

Governor's FY 2004-05 Budget Recommendation State Employee Funding Increases (millions of dollars)		
	Gross Appropriations	GF/GP Appropriations
Salary and Wage Costs.....	\$191.5	\$100.9
Insurance Costs	62.2	33.6
Retirement Costs.....	204.4	112.0
Workers' Compensation Costs.....	(3.3)	(2.9)
Building Occupancy Costs	(14.2)	(6.6)
Total Employee Costs.....	\$440.6	\$237.0
Proposed Employee Concessions	\$(147.9)	\$(76.2)
Net Employee Cost Increases.....	\$292.7	\$160.8

Tobacco Settlement Appropriations. The budget recommendation includes the appropriation of \$279.9 million of tobacco settlement funds from the Merit Award Trust Fund and the Tobacco Settlement Trust Fund. These tobacco settlement fund appropriations are summarized in [Table 13](#). The only major change in the appropriation of tobacco settlement funds from the appropriations in FY 2003-04, involves an increase in the Merit Award Trust Fund revenues appropriated to the State Medicaid program. The Governor is recommending that \$126.2 million of Merit Award Trust Fund and Tobacco Settlement Trust Fund revenues be appropriated for Medicaid. This represents a \$68.2 million increase from FY 2003-04. During FY 2003-04 this funding was directly appropriated from the Merit Award Trust Fund to the General Fund. All the remaining appropriations recommended from tobacco settlement funds in FY 2004-05 are very similar to the current-year appropriations.

Table 13

FY 2004-05 Tobacco Settlement Appropriations (actual dollars)			
Merit Award Trust Fund			
Department/Program	FY 2003-04 Year-to-Date	FY 2004-05 Gov's Rec.	Difference
Community Health			
Medicaid Base Funding	\$34,000,000	\$97,200,000	\$63,200,000
Education			
Michigan Education Assessment Program	0	13,685,200	13,685,200
Higher Education			
Merit Award Scholarships	67,000,000	67,000,000	0
Tuition Incentive Program	9,250,000	10,250,000	1,000,000
Nursing Scholarship Program	4,000,000	4,000,000	0
Operations Funding	9,500,000	9,500,000	0
Treasury			
Michigan Education Assessment Program	16,097,600	0	(16,097,600)
Merit Award Board	2,000,000	1,584,000	(416,000)
Tuition Incentive Program Administration	369,100	381,500	12,400
Michigan Education Savings Program	1,000,000	1,000,000	0
Information Technology	393,000	393,000	0
Transfer to General Fund	63,000,000	0	(63,000,000)
Total Merit Award Trust Fund Appropriations	\$206,609,700	\$204,993,700	(\$1,616,000)
Tobacco Settlement Trust Fund			
Department/Program	FY 2003-04 Year-to-Date	FY 2004-05 Gov's Rec.	Difference
Attorney General			
Legal Services	\$351,800	\$366,400	\$14,600
Community Health			
Senior Prescription Drug Program	30,000,000	25,500,000	(4,500,000)
Nursing Home Personal Needs Allowance	5,000,000	5,000,000	0
Senior Respite Care Services	5,000,000	5,000,000	0
Medicaid Base Funding	24,000,000	29,000,000	5,000,000
Labor and Economic Growth			
Life Sciences/Technology Tri-Corridor	0	10,000,000	10,000,000
Strategic Fund Agency			
Life Sciences/Technology Tri-Corridor	10,000,000	0	(10,000,000)
Transfer to General Fund	1,000,000	0	(1,000,000)
Total Tobacco Settlement Trust Fund Appropriations	\$75,351,800	\$74,866,400	(\$485,400)
Total Tobacco Settlement Appropriations	\$281,961,500	\$279,860,100	(\$2,101,400)

Program Transfers. The budget recommendation transfers the funding for several programs from a department in which the funding for the program was appropriated in FY 2003-04 to a new department in FY 2004-05. Table 14 provides a summary of these program transfers. These appropriation program transfers implement program transfers recommended by the Governor through Executive Orders shifting programs from one State department to another. The largest of these program transfers deal with the new Department of Labor and Economic Growth created by Executive Order 2003-18.

Table 14

Summary of Program Transfers					
From:	Fund Source	FY 2003-04 Transferred Out	To:	Fund Source	FY 2004-05 Gov's Rec.
Career Development	Gross GF/GP	\$461,595,400 24,335,000	Labor and Economic Growth	Gross GF/GP	\$461,595,400 24,335,000
Consumer and Industry Services			Community Health		
Health Regulatory Systems.....	Gross GF/GP	39,732,600 4,820,200	Health Regulatory Systems (E.O. 2003-18).....	Gross GF/GP	41,594,400 5,390,800
Bureau of Regulatory Services.....	Gross GF/GP	22,677,300 10,947,500	Family Independence Agency	Gross GF/GP	23,047,800 11,109,600
Remaining Programs in CIS.....	Gross GF/GP	542,231,900 197,700	Labor and Economic Growth	Gross GF/GP	542,231,900 197,700
Education			State		
Driver's Education Administrative Costs	Gross GF/GP	528,000 0		Gross GF/GP	528,000 0
Family Independence Agency			Labor and Economic Growth		
Commission for the Blind	Gross GF/GP	17,879,100 4,004,200		Gross GF/GP	17,939,200 4,064,000
Commission on Disability Concerns	Gross GF/GP	957,100 351,000	Labor and Economic Growth	Gross GF/GP	969,100 366,800
Real Estate	Gross GF/GP	113,400 113,400	Management and Budget	Gross GF/GP	113,400 113,400
Information Technology			Management and Budget		
MAIN Help Desk.....	Gross GF/GP	151,900 0		Gross GF/GP	151,900 0
			State		
In-house Systems.....	Gross GF/GP	698,500 0	In-house Systems.....	Gross GF/GP	698,500 0

Table 14 (continued)

Summary of Program Transfers					
From:	Fund Source	FY 2003-04 Transferred Out	To:	Fund Source	FY 2004-05 Gov's Rec.
Information Technology			School Aid		
Center for Educational Performance and Information (CEPI).....	Gross	13,500		Gross	13,500
	GF/GP	0		GF/GP	0
Labor and Economic Growth			Information Technology		
Unemployment Computer System ...	Gross	9,115,200		Gross	9,115,200
	GF/GP	0		GF/GP	0
Management and Budget			Labor and Economic Growth		
Michigan Strategic Fund.....	Gross	102,337,400		Gross	103,166,600
	GF/GP	38,380,100		GF/GP	39,145,100
State Police			Labor and Economic Growth		
Fire Fighter Training Council/Fire Marshal Programs	Gross	1,943,300		Gross	1,953,500
	GF/GP	1,708,300		GF/GP	1,718,500
Commercial Vehicle Information System Network	Gross	1,000,000	Information Technology		
	GF/GP	0		Gross	1,000,000
				GF/GP	0
Base Information Technology Functions	Gross	1,430,000	Information Technology		
	GF/GP	0	Base Information Technology Functions.....	Gross	1,430,000
				GF/GP	0
Treasury			Management and Budget		
Internal Audit	Gross	425,000		Gross	425,000
	GF/GP	425,000		GF/GP	425,000
Federal NAEP Grants.....	Gross	100,000	Education		
	GF/GP	0		Gross	120,000
				GF/GP	0
Educational Assessment Operations - MEAP	Gross	27,300,500	Education		
	GF/GP	0	Educational Assessment Operations - MEAP	Gross	24,968,900
				GF/GP	0

Agriculture. The FY 2004-05 budget recommendation represents a 23.4% increase in Adjusted Gross appropriations and a 4.1% increase in GF/GP appropriations. The significant increase in Gross appropriations is due to the appropriation of \$17.8 million of

increased Federal funds for the emerald ash borer eradication project. The GF/GP appropriation increase can be primarily attributed to employee cost adjustments.

Attorney General. The FY 2004-05 budget recommendation represents a 2.3% increase in Adjusted Gross appropriations and a 1.5% increase in GF/GP appropriations. The only major funding item contained in the recommendation is the funding for employee cost adjustments.

Capital Outlay. The FY 2004-05 budget recommendation represents a 1.9% increase in Adjusted Gross appropriations and a 7.5% increase in GF/GP appropriations. The major funding increase included in the budget is a \$19.0 million GF/GP funding increase for the projected debt service payments on bonds issued by the State Building Authority. The budget recommendation also includes the funding for three Department of Military and Veterans Affairs construction projects funded with Federal funds. These projects include a North Lansing headquarters building, a Camp Grayling National Guard headquarters building, and an expansion of the Michigan Air National Guard facility in Grand Ledge.

Civil Rights. The FY 2004-05 budget recommendation represents a 1.1% increase in Adjusted Gross appropriations and a 1.2% increase in GF/GP appropriations. The funding increases in the budget can be attributed to employee cost adjustments.

Civil Service. The FY 2004-05 budget recommendation represents a 12.4% increase in Adjusted Gross appropriations and a 0.6% decline in GF/GP appropriations. The recommendation consolidates certain human resources services through the creation of the Human Resources Service Center in the Department of Civil Service. This center will provide State employees with a central information source for questions regarding personnel issues. The Human Resources Service Center will be funded from user charges to other State departments and agencies. The proposed consolidation of human resources functions does not include the Legislature, the Judiciary, the Department of Attorney General, or the Department of State.

Community Colleges. The FY 2004-05 budget recommendation represents a 0.2% increase in Adjusted Gross and GF/GP appropriations. The recommendation is built on the assumption that all community colleges agree to no tuition increases in the balance of the 2003-04 academic school year and limit tuition increases in the 2004-05 academic school year to 2.3%. If the community colleges meet this tuition requirement, they will receive a 3.0% increase in their operational funding in FY 2003-04 and that increase will be built into their base operational funding for FY 2004-05. If they do not comply with the tuition restraint requirements, they will not receive the 3.0% increase in FY 2003-04 and their operational funding in FY 2004-05 will be reduced by 3.0%.

Community Health. The FY 2004-05 budget recommendation represents a 0.9% increase in Adjusted Gross appropriations and a 6.7% reduction in GF/GP appropriations. The recommended changes in the budget include three major types of changes. These changes are Medicaid base and fund source adjustments, Medicaid program reductions, and other fund source shifts. While the net result of all of these changes is a significant decrease in GF/GP appropriations, the amount of GF/GP and GF/GP equivalent funding

is actually increasing by almost \$400 million. The Governor's recommendation to place cigarette and estate tax revenue increases into the Medicaid Benefits Trust Fund means these funds are accounted for as State Restricted funds rather than GF/GP funds.

Medicaid Base and Fund Source Adjustments. The budget includes a \$450.3 million increase in Medicaid GF/GP funding. These cost increases consist of \$109.8 million for Medicaid base funding for physical health, mental health and substance abuse services, \$102.6 million for a reduction in the Federal Medicaid match rate, \$18.9 million from changes in Quality Assurance Assessment Program costs, and \$152.6 million from the phase-out of Medicaid special financing mechanisms. A final GF/GP funding increase is a \$66.4 million increase to meet Federal requirements on reimbursement rates paid to HMOs and Medicaid service offered by Community Mental Health boards.

Medicaid Program Reductions. The recommendation includes a total of \$64.3 million in GF/GP funding reductions in the Medicaid program. These reductions include the implementation of a quality assessment plan for group homes for the developmentally disabled, adjustments in the assessments paid to HMOs, elimination of coverage of nursing home hospital leave days, and a reduction in Medicaid physician emergency room reimbursement rates.

Fund Source Shifts. The recommendation includes three major fund source shifts, where Restricted and Tobacco Settlement Funds would be added to the budget, thus supplanting GF/GP revenues. The largest of these shifts takes \$419.1 million of tobacco tax revenues and dedicates these funds to the Medicaid Benefits Trust Fund. This \$419.1 million consists of the revenue from the proposed 75-cent-per-pack cigarette tax increase, the dedication of cigarette tax funds scheduled to be deposited into the Budget Stabilization Fund, and an increase in the amount of Merit Award Trust Fund revenues dedicated to fund the Medicaid program. In addition, the Governor is recommending that the \$94.3 million of revenues to be generated from the imposition of a State estate tax also be deposited into the Medicaid Benefits Trust Fund. The net impact of these proposed fund shifts is the use of State Restricted funds to offset \$577.1 million of existing GF/GP funding in the Medicaid program.

The budget recommendation also includes the appropriation of \$30.0 million of increased funding for the Healthy Michigan Fund. This funding would come from a portion of the 75-cent-per-pack cigarette tax increase. This change would increase funding for chronic disease prevention programs, smoking prevention programs, and maternal and children's health programs.

Corrections. The FY 2004-05 budget recommendation represents a 7.0% increase in Adjusted Gross appropriations and a 8.3% increase in GF/GP appropriations. The funding increases in the budget include the cost associated with the full-year funding of 1,000 additional prison beds, salary step increases for employees, increased funding for Hepatitis C testing and treatment, increases in parole and community placement programs, pharmaceutical cost increases, and a \$150.4 million GF/GP funding increase for employee cost adjustments. These cost increases are partially offset by savings from the closure of the Western Wayne women's prison and additional savings from using security technology enhancements to reduce staff. The budget is also built on assumptions concerning statutory changes that, if approved by the Legislature, will have the impact of reducing the need for prison bed capacity

by 400 beds. These statutory changes involve changes in the sentencing of probation violators and changes to limit the discretion judges have in deciding to send a convicted felon to State prison as opposed to a local jail option.

Education. The FY 2004-05 budget recommendation represents a 6.7% increase in Adjusted Gross appropriations and a 2.1% decrease in GF/GP appropriations. The large increase in Adjusted Gross appropriations reflects the transfer into the department of the Educational Assessment Program from the Department of Treasury and the \$27.3 million of funding for the program. The GF/GP funding changes are a combination of increased funding for employee cost adjustments and a modest decrease in funding for the projected cost of the school breakfast program.

Environmental Quality. The FY 2004-05 budget recommendation represents an 8.7% decrease in Adjusted Gross appropriations and a 28.8% decrease in GF/GP appropriations. The large funding decreases in the budget can be attributed to changes in the funding for environmental cleanup programs. The Environmental Response and the Environmental Protection Funds are used to support environmental cleanup projects. Revenue to these funds has been declining and appropriations cannot be sustained at the current fiscal year level. Two actions are taken in the budget recommendation to address this issue. The first is a fund shift of \$18.4 million where State Restricted funding from the Cleanup and Redevelopment Fund would replace program funding from other State Restricted appropriations. The second is the elimination of all funding in the annual budget for new environmental cleanup projects. This change reduces Adjusted Gross appropriations by \$21.7 million. Environmental cleanup projects during FY 2004-05 would be funded with approximately \$120 million of previously appropriated environmental cleanup funds not yet spent. The GF/GP funding decrease in the budget is a result of a proposal to replace \$16.3 million of GF/GP funding used as a State match for the State Water Pollution and Drinking Water Revolving Loan Fund with State funds generated from the issuance of State revenue bonds. The other major issue in the budget recommendation is the funding related to State employee cost adjustments.

Executive. The FY 2004-05 budget recommendation contains the same level of appropriations as the year-to-date appropriations for FY 2003-04.

Family Independence Agency. The FY 2004-05 budget recommendation represents a 9.7% increase in Adjusted Gross appropriations and a 3.4% increase in GF/GP appropriations. The budget reflects major changes in the use of Federal Temporary Assistance for Needy Families (TANF) block grant funds. TANF funds are used to replace other Federal funds, fund caseload increases, and increase the children's clothing allowance. The children's clothing allowance would increase from \$40 per school age child to \$50 per child for all ages. Other funding increases are for projected changes in foster care, adoption subsidy, food assistance, supplemental security income, and State disability assistance caseloads. The budget also reflects the replacement of one-time child support enforcement penalty refund revenues with GF/GP funding in the child support automation, State disability assistance caseload, and the funding of protective service workers. The 120 bed Sequoyah Center at the Maxey Boys Training School is closed as part of a plan to delete old facility beds, with youth and staff being moved to other facilities. The other major issue in the budget is the funding related to State employee cost adjustments.

Higher Education. The budget recommendation represents a 3.9% decrease in Adjusted Gross appropriations and 4.2% decrease in GF/GP appropriations. The recommendation is built on the assumption that all universities agree to no tuition increases in the balance of the 2003-04 academic school year and limit tuition increases in the 2004-05 academic school year to the rate of increase in the 2005 Detroit Consumer Price Index (CPI). Under current law, tuition increases are limited to 2.3%, the fiscal year 2004-05 estimated Detroit CPI increase; the Governor removes the reference to “fiscal” year. If the universities meet this tuition requirement, they will receive a 3.0% increase in their operations funding in FY 2003-04 and that increase will be built into their base operations funding for FY 2004-05. If they do not conform to the tuition restraint requirements, they will not receive the 3.0% increase in FY 2003-04 and their operations funding in FY 2004-05 will be reduced by 3.0%. The budget recommends the elimination of the \$64.8 million of funding for the Michigan Tuition Grant Program. This program provides need-based financial aid to approximately 32,500 students attending Michigan’s independent colleges and universities. The budget also includes two recommended adjustments to the Michigan Merit Award Scholarship Program. While these recommended changes are included in the FY 2004-05 budget recommendation, they will not have an impact on State expenditures on this program until FY 2005-06. The first change is a requirement that high school students who graduate beginning in June 2005, meet certain community service requirements to qualify for a Merit Award Scholarship. The second is the proposed elimination of the additional \$500 of Merit Award Scholarship funding for 7th and 8th grade students who qualified for a scholarship based on test scores. The first students who would be eligible for this funding will graduate from high school in June 2005.

History, Arts and Libraries. The budget recommendation represents a 3.9% increase in Adjusted Gross appropriations and a 7.4% increase in GF/GP appropriations. The major change in the budget is the funding of a new program called the Preservation and Access for Michigan Project. This program would allow for some of the rare historical documents maintained in libraries around the State to be made available statewide through digitization. These digital images would then be on-line through the Michigan Electronic Library. The budget also includes the continuation of special funding for the Detroit and Grand Rapids Public Libraries. These grants, which were funded with Federal funds in the current year will be funded with GF/GP appropriations. The final funding item in the budget is the funding of employee related cost adjustments.

Information Technology. The budget recommendation represents a 1.7% increase in Gross appropriations. The Department of Information Technology is completely funded with interdepartmental grants from other State departments. The budget recommendation includes the funding of \$1.1 million for the Human Resources Optimization Call Center, a \$0.5 million increase in funding for the Bureau of Retirement Systems, and \$0.7 million for Bureau of State Lottery costs. Reductions include a \$21.5 million saving from data center and telecommunication rates, equipment, and a reduction in contractual costs. The final funding item in the budget is the funding of employee related cost adjustments.

Judiciary. The budget recommendation represents a 0.1% decrease in Adjusted Gross appropriations and a 1.3% decrease in GF/GP appropriations. The budget reflects the loss of funding for three Federal grant programs, a reduction in State Restricted funding for the Court Equity Fund, and the elimination of one judgeship. The final funding item in the budget is the funding for employee related cost adjustments.

Labor and Economic Growth. The FY 2004-05 budget recommendation is the first year of recommended funding for this new department created by Executive Order 2003-18, which combined the Department of Consumer and Industry Services with the Department of Career Development and transferred the Strategic Fund Agency from the Department of Management and Budget. Compared with the funding levels in the previous structure, the budget represents a 8.2% increase in Adjusted Gross appropriations and a 57.8% increase in GF/GP appropriations. The budget reflects the appropriation of \$12.9 million of new Federal funding for unemployment programs and \$21.9 million of new Federal funding for job training, adult education, and vocational rehabilitation programs. The GF/GP funding increase reflects a funding shift in the Work First program from Federal funds to a \$39.9 million GF/GP funding increase. The budget also fully funds fire protection grants at \$15 million. These grants are awarded to communities that provide fire protection services for State-owned buildings. This funding will come from a combination of liquor purchase revolving fund revenue and fee revenue from the drivers responsibility legislation.

Legislature. The budget recommendation represents a 0.1% decrease in Adjusted Gross and GF/GP appropriations. The only change recommended from the current-year funding levels is a small adjustment in audit revenue to be received by the Office of the Auditor General.

Management and Budget. The budget recommendation represents a 4.4% increase in Adjusted Gross appropriations and a 3.6% increase in GF/GP appropriations. The budget includes adjustments related to property management costs, increases for the operation of the automated retirement system, savings from the restructuring of the long-term lease of the Cadillac Place State office building in Detroit, and other costs savings. The budget also reflects the proposed elimination of the line item appropriation for the motor transport revolving fund. Prior to FY 2003-04, this fund was treated as an off-budget item. The final funding item in the budget is the funding for employee related cost adjustments.

Military and Veterans Affairs. The budget recommendation represents a 6.9% increase in Adjusted Gross appropriations and a 3.4% increase in GF/GP appropriations. The budget reflects a \$125,000 GF/GP funding increase for the Youth Challenge Program. This change will allow for two schools with a goal of 50 graduates each. New Federal funding is provided for the operation and maintenance of military training sites around the State. Funding for the veterans service organization grants is continued at the current-year level. The final funding item in the budget is the funding for employee-related cost adjustments.

Natural Resources. The budget recommendation represents a 0.1% increase in Adjusted Gross appropriations and an 8.7% decrease in GF/GP appropriations. The major change recommended in the budget is the method by which the State pays payments in lieu of property taxes on certain State-owned lands. Under current law these payments are made from an appropriation that consists of a combination of State Restricted and GF/GP funding. The recommendation would fund these payments out of statutory State revenue sharing payments appropriated in the Department of Treasury. The budget also includes increased funding for snowmobile trail development, which would be funded with a scheduled increase in the snowmobile trail permit fee. The final funding item in the budget is funding for employee-related cost adjustments.

K-12 School Aid. The budget recommendation represents a 0.1% increase in Adjusted Gross appropriations and a 59.8% decrease in GF/GP appropriations. The major recommendations in the budget include maintaining the foundation allowance at \$6,700 per pupil. This would provide the base level of funding for local school districts and public school academies that they were initially expected to receive in FY 2003-04 before a pro-rata reduction in December 2004 reduced their per pupil funding levels by \$74. The budget also includes a recommendation to change the blended membership count from the current 80%/20% blend to a 50%/50% blend. Currently, a district's membership is determined by blending 80% of the current-year September pupil count with 20% of the prior-year February pupil count. This change would lead to an estimated \$43.0 million saving in foundation allowance payments. The Freedom to Learn program, which provides personal computer to junior high school students, would be funded with \$5.0 million of State funds. New programs recommended in the budget include \$1.0 million for incentive grants for school districts to consolidate. Districts that choose to consolidate would receive \$25 per pupil up to a maximum of \$500,000. Funding for intermediate school district operations is reduced by \$7.7 million. Of this reduction \$6.7 million would be redirected to intermediate school districts to operate a Great Parents, Great Start program for an age 0 to age 5 preschool program. The budget also proposes to reduce the foundation allowance by \$74 per pupil for all school districts whose foundation allowance exceeds \$9,000 per pupil. The final change to note is that local school districts will be required to pay a 1.88 percentage point increase of payroll into the Public School Employees Retirement System in FY 2004-05 as a result of actuarially required funding. This retirement funding change is the responsibility of the local school districts.

State. The budget recommendation represents a 4.5% increase in Adjusted Gross appropriations and an 8.2% decrease in GF/GP appropriations. The budget reflects the transfer of the driver education program to the Department of Education and the shift of \$1.0 million of funding from GF/GP revenue to State Restricted revenue for the mainframe computer replacement project. Other funding increases in the budget include GF/GP funding for the maintenance of the qualified voter file and State Restricted funding to implement changes to the notary public laws. The final funding item in the budget is funding for State employee cost adjustments.

State Police. The budget recommendation represents a 4.8% increase in Adjusted Gross appropriations and a 4.6% increase in GF/GP appropriations. The budget includes a \$1.0 million GF/GP funding increase to be used to reduce the backlog in DNA profiling cases at the State's crime laboratories. Funding has been included in the budget to fund the full-year costs of a State trooper school held in the summer of 2004, but no funding is included for a new trooper school in FY 2004-05. The six State Police regional dispatch centers would be consolidated into four centers under the budget proposal. The final funding item in the budget is funding for State employee related cost adjustments.

Transportation. The budget recommendation represents a 5.9% increase in Adjusted Gross appropriations. The budget includes a proposal to redirect one-half of the revenue from one cent of the gasoline tax from State bridge projects to local bridge projects. This change would result in a \$25.6 million funding increase for local bridge projects. The budget also reflects a \$35.7 million increase in the level of debt service payments on transportation bonds, a \$163.3 million increase in Federal funds for State and local road and bridge projects, and a \$1.3 million funding increase to support the administrative costs in the Bureau of Multi-Modal Transportation Services. The budget includes funding for State employee cost adjustments.

Treasury-Debt Service. The budget recommendation represents a 44.7% increase in Adjusted Gross appropriations and a 27.4% increase in GF/GP appropriations. The increase is a result of substantial increases in the debt service requirements for outstanding State of Michigan general obligation bonds. Debt service requirements on Quality of Life bonds will increase from \$37.5 million to \$59.7 million and the debt service requirements on Clean Michigan Initiative bonds will increase from \$16.0 million to \$19.1 million. Part of the funding for Quality of Life bonds also will shift from GF/GP funding to State Restricted funding. This shift to Cleanup and Redevelopment Fund revenues will result in a \$10.0 million GF/GP appropriation reduction.

Treasury-Operations. The budget recommendation represents a 3.9% decrease in Adjusted Gross appropriations and a 5.4% decrease in GF/GP appropriations. The budget reflects the transfer of \$27.3 million of Federal and State Restricted funding for the administration of the Michigan Educational Assessment Program to the Department of Education. Increases of State Restricted funding in the budget include distributions from the Convention Facilities Fund, commercial mobile radio service payments and funding from the Michigan Transportation Fund. The amount of GF/GP appropriations is affected by a reduction in qualified agricultural loan grants and an increase in funding for the senior citizen tax exemption payments and renaissance zone reimbursements.

Payments to Local Units of Government

The Governor's FY 2004-05 budget recommendation includes \$15.5 billion of estimated payments to local units of government. This exceeds the required level of payments to local units of government pursuant to Article IX, Section 30 of the State Constitution of 1963 by \$2.8 billion. Table 15 provides a summary of this estimate.

Table 15 State Payments to Local Units of Government Article IX, Section 30 Requirement (millions of dollars)	
	FY 2004-05 Estimate
State Spending from State Resources.....	\$25,997.6 ^{a)}
Required Payments to Local Units of Government (48.97%).....	12,731.0
Actual or Estimated Payments to Locals	15,526.3
Actual Percentage of Total State Spending	59.72%
Surplus of Section 30 Payments.....	2,795.3
^{a)} Does not include \$30.0 million of Federal aid counted as GF/GP revenue.	

State Employment

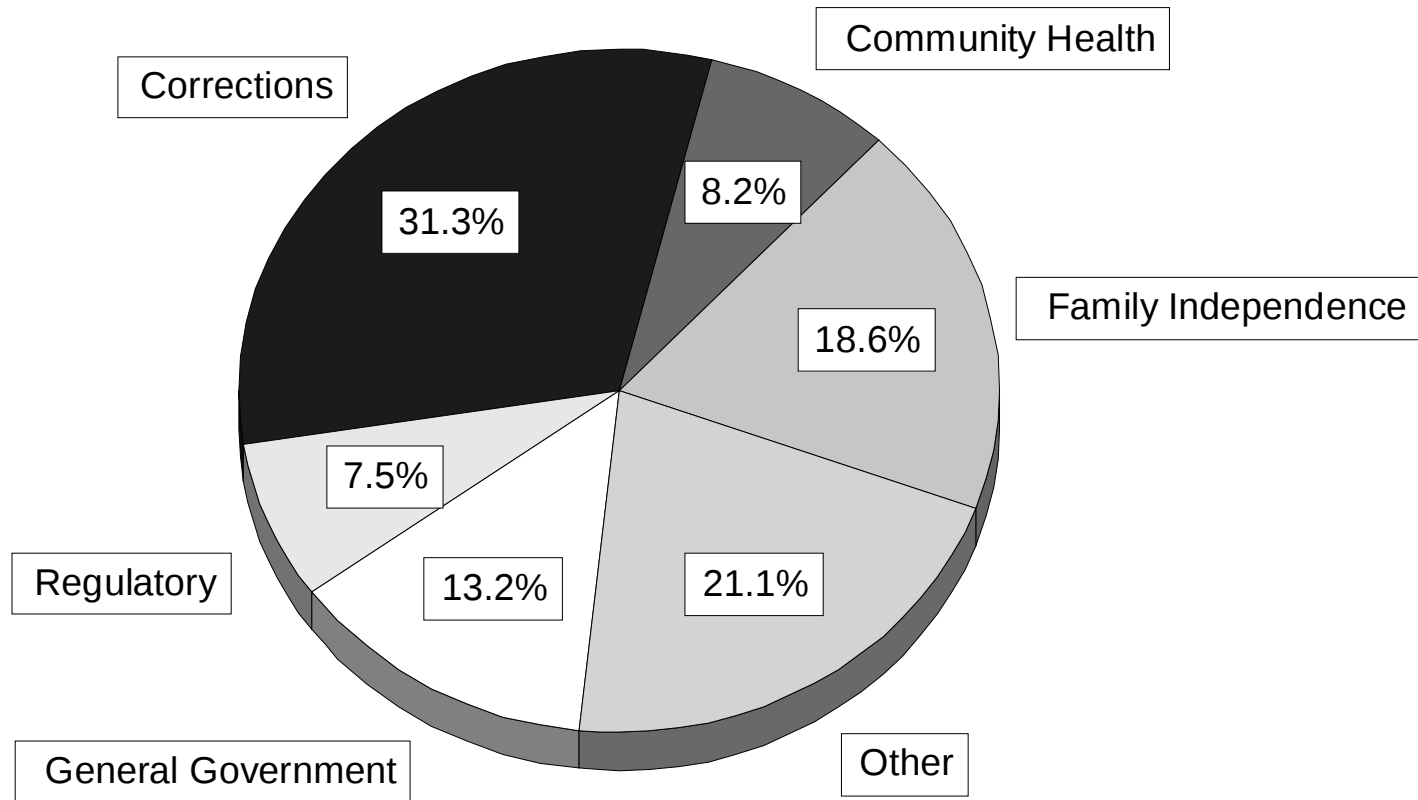
Table 16 and Figure E provide a comparison of classified and full-time equated (FTE) positions recommended by the Governor with the appropriated levels of FTEs for FY 2003-04. The Governor's FY 2004-05 recommendation includes the funding for 56,793.1 FTEs. This represents an 865.5 FTE decline or 1.5% below the current fiscal year level. The majority of these FTE reductions simply reflect an effort to correlate the appropriated levels of FTEs more closely with the actual number of positions currently filled in State departments.

Table 16
Full-Time Equated Positions
FY 2003-04 Versus Governor's Recommendation

Department/Budget Area	FY 2003-04 Year-to-Date Appropriations	FY 2004-05 Governor's Recommendation	Position Change	Percent Change
Agriculture	563.0	709.0	146.0	25.9%
Attorney General	562.0	556.0	(6.0)	(1.1)
Career Development	989.5	0.0	(989.5)	(100.0)
Civil Rights.....	137.0	136.0	(1.0)	(0.7)
Civil Service	211.5	240.5	29.0	13.7
Community Health	4,382.3	4,674.0	291.7	6.7
Consumer and Industry Services	3,470.0	0.0	(3,470.0)	(100.0)
Corrections	18,296.7	17,788.6	(508.1)	(2.8)
Education.....	433.1	394.0	(39.1)	(9.0)
Environmental Quality	1,605.7	1,572.2	(33.5)	(2.1)
Executive	74.2	74.2	0.0	0.0
Family Independence Agency	10,774.6	10,590.1	(184.5)	(1.7)
History, Arts and Libraries	248.5	232.0	(16.5)	(6.6)
Information Technology.....	1,749.4	1,756.4	7.0	0.4
Judiciary	582.5	582.5	0.0	0.0
Labor and Economic Growth.....	0.0	4,238.0	4,238.0	0.0
Management & Budget (Operations).....	716.0	723.0	7.0	1.0
Military Affairs.....	1,072.0	1,016.0	(56.0)	(5.2)
Natural Resources.....	2,088.5	2,070.5	(18.0)	(0.9)
State	1,849.8	1,853.8	4.0	0.2
State Police	2,987.0	2,948.0	(39.0)	(1.3)
Strategic Fund Agency	200.0	0.0	(200.0)	(100.0)
Transportation	3,050.3	3,044.3	(6.0)	(0.2)
Treasury (Operations)	1,615.0	1,594.0	(21.0)	(1.3)
TOTAL POSITIONS.....	57,658.6	56,793.1	(865.5)	(1.5)%

Figure E

Full-Time Equated Positions FY 2004-05 Governor's Recommendation



Projected Year-End Balances

Combining the Governor's FY 2004-05 appropriation recommendations with the consensus revenue estimate and recommended tax policy changes leads to updated estimates of the FY 2004-05 GF/GP and School Aid Fund year-end balances. Assuming that all of the Governor's revenue and appropriation recommendations are enacted, the FY 2004-05 GF/GP budget will close the fiscal year with a \$5.1 million balance. The FY 2004-05 School Aid Fund budget will close the fiscal year with a zero balance. Tables 17 and 18 provide a summary of these recommendations.

Table 17 FY 2004-05 General Fund/General Purpose Revenues, Expenditures and Year-End Balance (millions of dollars)	
	<u>Governor's Recommendation</u>
Revenues:	
Beginning Balance	\$ 0.0
Ongoing Estimated Revenue	7,822.8
Enacted Revenue Adjustments:	
Enhanced Tax Enforcement Revenue	85.1
Driver Responsibility Legislation.....	121.5
Driver License Fee Legislation	25.0
Escheats Law Change	<u>15.0</u>
Subtotal Enacted Revenue Adjustments	246.6
Proposed Revenue Adjustments:	
Increase Liquor Markup to 74%.....	31.8
Freeze Revenue Sharing	355.4
Suspend County Revenue Sharing Payments.....	183.5
Adjust Interfund Borrowing Costs	<u>20.0</u>
Subtotal Proposed Revenue Adjustments	590.7
Total Estimated Revenue.....	\$8,660.1
Expenditures:	
Governor's Recommendation.....	\$8,655.0
Projected Year-End Balance	\$ 5.1

Table 18 FY 2004-05 School Aid Fund Budget Revenues, Expenditures and Year-End Balance (millions of dollars)	
	<u>Governor's Recommendation</u>
Revenue:	
Beginning Balance	\$ 0.0
Ongoing Estimated Restricted Revenue	10,998.5
<u>Other Revenue Adjustments:</u>	
GF/GP Grant.....	131.8
Federal Aid.....	1,314.4
Enhanced Tax Enforcement Revenue.....	35.5
<u>Proposed Revenue Adjustments:</u>	
Liquor Markup Increase	1.7
Payment in Lieu of Taxes.....	(2.0)
Subtotal Other Revenue Adjustments	1,481.4
Total Estimated Revenue.....	\$12,479.9
Expenditures:	
Governor's Recommendation.....	\$12,479.9
Projected Year-End Balance	\$ 0.0

ECONOMIC AND REVENUE FORECAST

Economic Forecast

The Governor's proposed budget for FY 2004-05 is based on an economic forecast that assumes that the protracted weak level of economic activity that has occurred since the end of the 2001 recession, will finally come to an end in 2004 and the pace of the renewed economic expansion will continue to improve in 2005. In particular, the improvement in economic activity that began nationally in the second half of 2003 is expected to spread to the labor market in 2004. It is forecasted that the number of people employed will increase in the next two years for both the U.S. and Michigan economies. This economic forecast is summarized in Table 19 and is the consensus forecast adopted by the Treasury Department, Senate Fiscal Agency, and House Fiscal Agency at the January 14, 2004, Consensus Revenue Estimating Conference.

U.S. Economy. Nationally, economic activity experienced renewed growth during the latter half of 2003. Some of the highlights of recent improvements in economic activity include a rebound in the stock market, an increase in manufacturing activity, a decline in initial unemployment claims, increases in the index of leading economic indicators, and continued low interest rates. Employment even began to rebound in the latter part of 2003, but the increases were very small. The forecast is that the meager improvements in employment that transpired in the second half of 2003, will lead to stronger increases in employment in 2004 and 2005.

Real Gross Domestic Product (GDP) will increase an estimated 4.6% in 2004, after growing 3.1% in 2003. In 2005, real GDP will grow by an estimated 3.7%.

Inflation, as measured by the U.S. Consumer Price Index, is expected to stay low and under control through 2005.

The unemployment rate will average 6.1% in 2004, which will be up from 5.8% in 2003, and then as the pace of employment gains improves, the unemployment rate will fall to an estimated 5.6% in 2005.

Light vehicle sales will total an estimated 16.8 million units in 2004, after totaling 16.6 million units in 2003. In 2005, light vehicle sales will edge up slightly to an estimated 16.9 million units.

Michigan Economy. The Michigan economy has had a much more difficult time pulling out of the weak economic activity that has prevailed since the end of the 2001 recession. While there have been some encouraging improvements in some key economic indicators nationally, there has not been much good news from the Michigan economy. The labor market has been very weak, particularly in the manufacturing sector. However, given the improved level of economic activity that is forecast for the U.S. economy, it is estimated that Michigan's economy also will finally turn the corner to renewed economic growth in 2004 and then experience even stronger growth in 2005.

Wage and salary employment is expected to increase 0.5% to 4.45 million workers in 2004, which will be an improvement from the 1.2% decline in employment that occurred in 2003. In 2005, the pace of employment growth is expected to increase to 1.8%, which will push employment up to 4.53 million workers. These increases in employment are the key factors to Michigan's experiencing renewed economic growth in 2004 and 2005.

The unemployment rate will edge up to 7.2% in 2004, from 7.1% in 2003, and then fall to an estimated 6.4% in 2005.

Personal income will increase 4.5% to an estimated \$325.7 billion in 2004. In 2003, personal income increased only 2.6%. In 2005, the rate of increase will accelerate to an estimated 5.9%, which will push personal income up to \$344.9 billion.

Table 19**Consensus Economic Forecast: 2004 and 2005
January 14, 2004**

	Calendar 2003	% Change from Prior Year	Calendar 2004 Forecast	% Change from Prior Year	Calendar 2005 Forecast	% Change from Prior Year
United States:						
Real Gross Domestic Product (billions of chained 1996 dollars)	\$9,731	3.1%	\$10,178	4.6%	\$10,555	3.7%
Consumer Price Index (1982-94=100)	184.0	2.3	187.5	1.9	192.2	2.5
3-Month Treasury bills (Interest Rate, %)	1.0	---	1.5	---	2.9	---
Unemployment Rate (Civilian - %)	5.8	---	6.1	---	5.6	---
Light Vehicle Sales (millions of units)	16.6	(0.6)	16.8	1.2	16.9	0.6
Michigan:						
Wage and Salary Employment (thousands)	4,424	(1.2)	4,446	0.5	4,526	1.8
Unemployment Rate (Civilian - %)	7.1	---	7.2	---	6.4	---
Personal Income (millions of dollars)	\$311,667	2.6	\$325,692	4.5	\$344,908	5.9
Real Personal Income (millions of 1982-84 \$s)	\$170,296	0.3	\$174,641	2.6	\$180,611	3.4
Detroit Consumer Price Index (1982-84=100)	183.0	2.3	186.5	1.9	191.0	2.4

Revenue Estimates

Based on the economic forecast summarized above, it is estimated that revenue totaling \$38.65 billion will be available in FY 2004-05 to support Governor Granholm's proposed budget. This represents a 0.4% increase from the revised revenue estimate for FY 2003-04. This total State government revenue includes revenue from taxes, fees, interest, licenses and permits, penalties, fines, Federal aid, carryover balances, and the Governor's proposed tax policy changes. Table 20 presents the overall State budget revenue estimates for FY 2003-04 and FY 2004-05, broken down by major fund.

Table 20

Governor's Projected Total State Revenue: FY 2003-04 and FY 2004-05
(dollars in millions)

Fund	FY 2002-03 Final	FY 2003-04 Estimated	% Change FY '04/FY '03	FY 2004-05 Estimated	% Change FY '05/FY '04
General Fund/General Purpose					
Beginning Balance	\$ 114.5	\$ 174.0	52.0%	\$ 0.0	(100.0)%
Revenue From Ongoing Sources ¹⁾	7,957.7	7,782.7	(2.2)	7,822.8	0.5
Proposed Liquor Price Markup Increase	0.0	0.0	---	31.8	---
Proposed Revenue Sharing Savings & Other	0.0	0.0	---	558.9	---
One-Time Revenue Adjustments & Other	941.8	887.1	(5.8)	246.6	(72.2)
Total GF/GP Revenue	\$9,014.0	\$8,843.8	(1.9)	\$8,660.1	(2.1)
School Aid Fund:					
Beginning Balance	237.0	113.7	(52.0)	0.0	(100.0)
Ongoing Earmarked Tax & Lottery Revenue ¹⁾	10,260.5	10,584.3	3.2	10,998.5	3.9
Proposed Tax Changes	0.0	0.0	---	(0.3)	---
One-Time Revenue Adjustments	616.9	33.6	(94.6)	35.5	5.7
Other Revenue (GF Grant, Federal Aid . . .)	1,337.7	1,644.4	22.9	1,446.2	(12.1)
Total SAF Revenue with Beginning Balance	\$12,452.1	\$12,376.0	(0.6)	\$12,479.9	0.8
Other Funds:					
General Fund/Special Purpose:					
Ongoing Revenue	13,061.7	12,823.9	(1.8)	12,351.3	(3.7)
Proposed Tax Increases:					
Tobacco Tax Increase to Medicaid Trust	0.0	0.0	---	265.0	---
Tobacco Tax Increase to Healthy Michigan	0.0	0.0	---	30.0	---
Estate Tax Increase to Medicaid Trust	0.0	0.0	---	94.4	---
Subtotal General Fund/Special Purpose	\$13,061.7	\$12,823.9	(1.8)	\$12,740.7	(0.6)
Transportation Funds	3,907.2	4,560.1	16.7	4,626.9	1.5
Other Special Revenue Funds:					
Beginning Balances	173.7	105.1	(39.5)	105.1	0.0
Revenue Current Period	1,055.2	783.1	(25.8)	752.5	(3.9)
Subtotal Other Special Revenue Funds	\$1,228.9	\$888.2	(27.7)	\$857.6	(3.4)
Other Revenue:					
Ongoing Other Revenue	317.7	370.2	16.5	376.2	1.6
Liquor Markup Increase to Fire Protection	0.0	0.0	---	3.7	---
Liquor Markup Increase to Convention & LPRF	0.0	0.0	---	2.3	---
Subtotal Other Revenue	\$317.7	\$370.2	16.5	\$382.2	3.2
Total Other Funds with Beginning Balance	\$18,515.5	\$18,642.4	0.7	\$18,607.4	(0.2)
Gross Revenue Current Period	\$39,981.6	\$39,862.2	(0.3)	\$39,747.4	(0.3)
Less Interfund Transfers	(2,130.6)	(1,351.1)	(36.6)	(1,096.6)	(18.8)
Gross Revenue with Beginning Balances	\$37,851.0	\$38,511.1	1.7%	\$38,650.8	0.4%

1) Estimates adopted at the January 14, 2004, Consensus Revenue Estimating Conference.

Source: Governor's Executive Budget for FY 2004-05 and Senate Fiscal Agency.

General Fund/General Purpose and School Aid Fund

Two of the major funds in the overall State budget are the General Fund/General Purpose (GF/GP) and School Aid Fund (SAF) budgets. These two funds account for an estimated \$21.0 billion, or 54% of the total revenue estimated for FY 2004-05. A breakdown of the GF/GP and SAF revenue estimates for FY 2003-04 and FY 2004-05, is presented in Tables 21 and 22. These GF/GP and SAF revenue estimates are the consensus estimates adopted by the Granholm Administration, Senate Fiscal Agency, and House Fiscal Agency at the January 14, 2004, Consensus Revenue Estimating Conference. These estimates include baseline revenue (which is the revenue that would be realized if there were no changes in the tax structure from one year to the next), the fiscal impact of enacted tax changes and one-time revenue adjustments, grants and transfers, Federal aid, and beginning carry-over balances, and also include the Governor's proposed tax increases described at the end of this section.

General Fund/General Purpose Revenue. As shown in Table 22, GF/GP revenue is expected to total \$8.66 billion in FY 2004-05, which is down 2.1% from the FY 2003-04 revised estimate. The major reasons for this decline are: 1) revenue from ongoing sources is expected to be down \$35 million, or 0.4%, and 2) there is not expected to be any balance carried over from FY 2003-04, while FY 2003-04 had a carry-over beginning balance of \$174 million. In addition, of the \$429 million in tax increases proposed by the Governor, only \$31.8 million from the proposed liquor price markup increase would go to GF/GP revenue. The proposed budget adjustments primarily reflect the increase in sales tax revenue that would accrue to the General Fund due to the Governor's proposal to reduce revenue sharing payments to local governments.

School Aid Fund. Total School Aid Fund revenue available for spending in FY 2004-05 will total an estimated \$12.48 billion, and is summarized in Table 18. The SAF revenue estimate for FY 2004-05 includes ongoing earmarked tax and lottery revenue totaling an estimated \$11.0 billion, a grant from the GF/GP budget of \$131.8 million, Federal aid of \$1.31 billion, and revenue from increased tax enforcement totaling \$35.5 million. The SAF also would receive an additional \$1.7 million in revenue from the 4% liquor tax due to the Governor's proposed increase in the liquor price markup, but it would lose \$2.0 million in State education property tax revenue due to a proposal to eliminate this tax on certain State-owned lands.

Table 21

General Fund/General Purpose Revenue Estimates
FY 2003-04 and FY 2004-05
(millions of dollars)

	FY 2003-04	FY 2004-05	Percent Change
Beginning Balance.....	\$174.0	\$0.0	---
Consensus Estimates for Ongoing Revenue Sources ¹⁾			
Taxes:			
Net Income Tax	3,918.8	3,994.1	1.9%
Single Business Tax	1,878.7	1,962.5	4.5
Sales.....	114.2	119.4	4.6
Use	838.4	867.7	3.5
Cigarette	286.2	128.0	(55.3)
Insurance Company Premiums	247.0	261.0	5.7
Telephone & Telegraph	120.6	120.6	0.0
Estate	70.0	34.0	(51.4)
All Other Taxes	157.8	156.6	(0.8)
Subtotal Taxes.....	7,631.7	7,643.9	0.2
Nontax Revenue	225.8	178.8	(20.8)
Total Current Period GF/GP Consensus Revenue Estimates	\$7,857.5	\$7,822.7	(0.4)
Enacted Revenue Adjustments ²⁾	812.3	246.7	(69.6)
Proposed Liquor Markup Increase	0.0	31.8	----
Proposed Budget Adjustments ³⁾	0.0	558.9	----
TOTAL GF/GP REVENUE W/ BEGINNING BALANCE	\$8,843.8	\$8,660.1	(2.1)%

¹⁾ Estimates adopted at the January 14, 2004, Consensus Revenue Estimating Conference.

²⁾ Includes the following: FY 2003-04 - \$289.7 million in increased sales tax revenue due to reduced revenue sharing payments, \$169.0 million in one-time Federal aid, \$65.0 million in bad driver assessments, \$25.9 million in increased driver license fees, \$55.1 million in increased tax collection enforcement, \$15.0 million in additional revenue from escheated property, \$76.6 million from the sale of State property, \$105.0 million in lapsed revenue, \$10 million transferred from the Employment Security Fund, and \$1.0 million from teacher certification fees. FY 2004-05 - \$121.5 million in bad driver assessments, \$25.0 million in increased driver license fees, \$85.1 million in increased tax enforcement, and \$15.0 million in additional escheated property.

³⁾ Includes the following: FY 2004-05 -\$538.9 million in increased sales tax due to revenue sharing reductions, and \$20 million savings in interfund borrowing costs.

Table 22

School Aid Fund Revenue Estimates
FY 2003-04 and FY 2004-05
(millions of dollars)

	FY 2003-04	FY 2004-05	Percent Change
Beginning Balance	\$113.7	\$0.0	(100.0)%
Consensus Estimates for Earmarked Tax & Lottery Revenue: ¹⁾			
Sales Tax & Use Tax.....	5,243.8	5,463.0	4.2
Income Tax	1,899.5	1,985.9	4.5
State Education Property Tax.....	1,745.2	1,858.2	6.5
Real Estate Transfer Tax.....	274.7	273.0	(0.6)
Tobacco Taxes.....	479.7	472.8	(1.4)
Other Tax Revenue	<u>306.6</u>	<u>310.6</u>	<u>1.3</u>
Subtotal Taxes	\$9,949.5	\$10,363.5	4.2%
Lottery	635.0	635.0	0.0
Subtotal Earmarked Tax & Lottery Consensus Estimate	\$10,584.5	\$10,998.5	3.9%
GF/GP Grant	327.7	131.8	(59.8)
One Time Revenue & Enhanced Tax Collections ²⁾	33.6	35.5	5.7
Federal Aid.....	1,316.7	1,314.4	(0.2)
Total Current Period SAF Revenue.....	\$12,262.5	\$12,480.2	1.8%
Proposed Tax Policy & Other Revenue Changes ³⁾	\$0.0	(\$0.3)	----
TOTAL SAF REVENUE W/ BEGINNING BALANCE	\$12,376.2	\$12,479.9	0.8%

¹⁾ Estimates adopted at the January 14, 2004, Consensus Revenue Estimating Conference.

²⁾ Includes the following: FY 2003-04 - \$5.0 million from personal property tax amnesty program and \$28.6 million from increased tax enforcement. FY 2004-05 - \$35.5 million from increased tax enforcement.

³⁾ Includes the following: FY 2004-05 - Loss of \$2.0 million due to eliminating State education property taxes on certain State-owned lands, and \$1.7 million from 4% liquor tax due to increase in liquor markup.

Tax Policy Changes

The Governor's budget proposes several tax policy changes including increasing the tobacco taxes, increasing the estate tax, and increasing the liquor price markup. Each of these proposed tax increases is described below and their estimated fiscal impacts are summarized in Table 23.

Table 23

Governor's Proposed Tax Policy Changes: FY 2004-05 Estimated Fiscal Impact by Fund (dollars in millions)							
Proposal	GF/GP	SAF	Medicaid Trust Fund	Healthy MI Fund	Fire Protection Grants	Other	Total
Tobacco Tax Increase	\$0.0	\$0.0	\$265.0	\$30.0	\$0.0	\$0.0	\$295.0
Estate Tax Increase	0.0	0.0	94.4	0.0	0.0	0.0	94.4
Liquor Price Markup Increase:							
Liquor Profits Increase	\$30.1	\$0.0	\$0.0	\$0.0	\$3.7	\$0.0	\$33.8
Liquor Specific Taxes	<u>1.7</u>	<u>1.7</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>2.3</u>	<u>5.7</u>
Subtotal Liquor Price Markup	\$31.8	\$1.7	\$0.0	\$0.0	\$3.7	\$2.3	\$39.5
Total Tax Increases	\$31.8	\$1.7	\$359.4	\$30.0	\$3.7	\$2.3	\$428.9

Tobacco Tax Increase

Current Law. Michigan's current tax on cigarettes is \$1.25 per pack and the tax on other tobacco products (cigars, chewing tobacco) is 20% of the wholesale price. Michigan's cigarette tax ranks 10th highest among the 50 states. These taxes were last increased in August 2002, when the cigarette tax was increased \$0.50 per pack and the tax on other tobacco products was increased from 16% to 20% of the wholesale price. Based on the consensus revenue estimates, these current taxes on tobacco products will generate an estimated \$864 million in FY 2004-05.

Proposed Increase. The Governor is proposing a \$0.75 per pack increase in the cigarette tax, from the current \$1.25 per pack to \$2.00 per pack, and an increase in the tax on other tobacco products from 20% to 32% of the wholesale price. Both of these increases would go into effect on October 1, 2004. In addition, these tax increases would be assessed on all tobacco products held in inventory by businesses on October 1, 2004. These tax increases, along with the tax on inventories, would generate an estimated \$295 million in FY 2004-05. The Governor is proposing that \$265 million of this increase go to the Medicaid Benefit Trust Fund and \$30 million to the Healthy Michigan Fund.

Estate Tax Increase

Current Law. Michigan's estate tax is currently directly linked to the Federal estate tax, because the Federal estate tax includes a credit for taxes an estate pays in state death taxes and Michigan's estate tax is equal to the maximum amount allowed under this

Federal credit. However, the Federal tax is being phased out, which means that Michigan estate tax also is being phased out. Federal legislation enacted in 2001, phases out the Federal estate tax from 2002 to 2010, but it also phases out the state death tax credit from 2002 to 2005. As a result, under current law, Michigan's estate tax will be completely eliminated on January 1, 2005, although revenue from the tax will continue through the end of FY 2004-05. Due to the phased elimination of the Federal estate tax and the state death tax credit, Michigan's estate tax revenue, which totaled \$185 million in FY 1999-2000, will decline to an estimated \$34 million in FY 2004-05 and will probably be close to zero in FY 2005-06.

Proposed Increase. Effective July 1, 2004, the Governor is proposing that Michigan's estate tax be decoupled from the current Federal estate tax by linking it permanently to most of the provisions that were in the Federal estate tax in 2001 (which were the provisions in place just before the phase-out of the Federal tax began). This new tax would include the following provisions:

- Estates valued at less than \$1 million would not have to pay the tax.
- Estates valued at more than \$1 million would pay a tax equal to the maximum Federal credit they could have claimed in 2001, which on average would equate to a tax of 5.3% of the value of the estate.
- Assets transferred to a spouse would continue to be totally exempt from the tax.
- Family-owned businesses, including farms, would be exempt from the estate tax.

The Department of Treasury estimates that about 1% of decedents' estates, which would currently total about 900 estates, would be subject to this proposed decoupled estate tax each year. It is estimated that this change in the estate tax would generate an additional \$94 million in FY 2004-05, and the Governor proposes that this additional revenue be deposited into the Medicaid Benefits Trust Fund.

At least 18 other states have already decoupled from the Federal estate tax.

Liquor Price Markup Increase

Current Law. The State of Michigan, through the Liquor Control Commission, regulates the price of liquor. Under current law, the price of liquor equals the price charged by liquor manufacturers plus a price markup of 65% for all liquor excluding beer and wine. The price of liquor paid by consumers also reflects three State specific taxes, each assessed at 4.0% of the price of liquor, plus a specific tax of 1.85% assessed on the price of liquor purchased for off-premises consumption. Proceeds from the sale of liquor are deposited into the Liquor Purchase Revolving Fund and the profits are transferred to the General Fund. In FY 2004-05, liquor profits are expected to generate \$121 million for the General Fund. The three 4.0% specific taxes are earmarked to the General Fund, School Aid Fund, and Convention Facility Development Fund, and each of these taxes is expected to generate about \$31.6 million in FY 2004-05. The 1.85% specific tax goes to the Liquor Purchase Revolving Fund, and its revenue is expected to total about \$11 million in FY 2004-05.

Proposed Increase. The Governor is proposing that the State's markup in the price of liquor be increased from 65% to 74%. This would increase the State's liquor profit by an estimated \$33.8 million in FY 2004-05. In addition, this increase in the price of liquor would increase the revenue generated from each of the three 4.0% specific taxes, by an estimated \$1.7 million, and the 1.85% tax would generate an additional \$0.6 million. It is proposed that the General Fund would receive \$30.1 million in increased profits, plus \$1.7 million from the 4.0% specific tax, for a total of 31.8 million. The remaining \$3.7 million in new profits would be used to finance fire protection grants to local governments. The School Aid Fund and Convention Facility Development Fund each would receive an additional \$1.7 million from its respective 4.0% specific taxes, and the Liquor Purchase Revolving Fund would receive an additional \$0.6 million from its 1.85% tax.



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