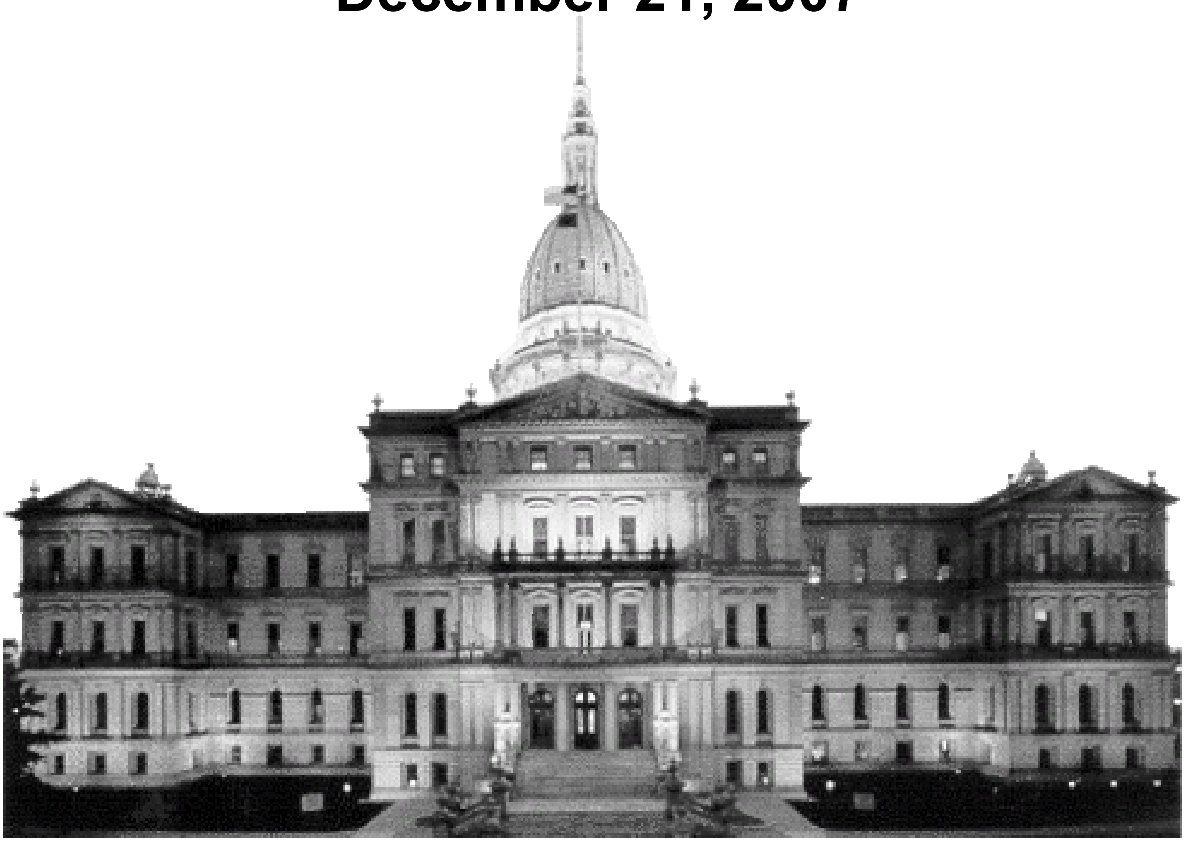
Senate Fiscal Agency

MICHIGAN'S ECONOMIC OUTLOOK AND BUDGET REVIEW

FY 2006-07, FY 2007-08, & FY 2008-09

December 21, 2007



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www.senate.michigan.gov/sfa

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ACKNOWLEDGEMENT

This Economic Outlook and Budget Review was prepared and written by Gary S. Olson, Director, Jay Wortley, Senior Economist, and David Zin, Economist, of the Senate Fiscal Agency. Karen Hendrick, Executive Secretary, coordinated the production of this report.

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ECONOMIC FORECAST

The U.S. economy, as measured by inflation-adjusted gross domestic product, is estimated to have grown 2.2% in 2007 and is predicted to expand 2.0% in 2008 and 2.8% in 2009. Light vehicle sales are estimated to have declined slightly to 16.0 million units in 2007 and are forecasted to decline to 15.8 million units in 2008 before rising to 16.3 million units in 2009. The unemployment rate is estimated to have fallen slightly to 4.5% in 2007 and is expected to rise to 4.9% in 2008 and 5.1% in 2009, while the consumer price index is estimated to have grown by 2.7% in 2007, and to grow 3.2% in 2008 and 2.8% in 2009.

The Michigan economy, as measured by inflation-adjusted personal income, is estimated to have grown 1.4% in 2007, and then is expected to decline 1.4% in 2008 before growing 0.4% in 2009. Wage and salary employment is estimated to have declined 1.4% during 2007, and is predicted to fall another 1.9% in 2008 and 0.9% in 2009.

REVENUE FORECAST

In FY 2006-07, General Fund/General Purpose (GF/GP) and School Aid Fund (SAF) revenue totaled $19.47 billion, representing a 0.6% increase from FY 2005-06. General Fund/General Purpose revenue was up 0.6% to $8.32 billion and SAF revenue increased 0.6% to $11.15 billion.

In FY 2007-08, GF/GP and SAF revenue will total an estimated $20.54 billion, which is up 5.5% from FY 2006-07. General Fund/General Purpose revenue will increase 10.4% to an estimated $9.18 billion, while SAF revenue will increase 1.8% to $11.36 billion. Most of this growth will be due to the increase in the income tax and the surtax on the Michigan business tax. Compared with the revenue estimate on which the FY 2007-08 enacted budget was based, the GF/GP revenue estimate is down $293.7 million and the SAF revenue estimate is down $132.7 million.

In FY 2008-09, GF/GP and SAF revenue will total an estimated $21.0 billion. This initial revenue estimate for FY 2008-09 is up 2.3% from the revised estimate for FY 2007-08. General Fund/General Purpose revenue will decline 0.6%, to an estimated $9.13 billion, due in part to the new earned income tax credit. School Aid Fund revenue will increase an estimated 4.6% to $11.88 billion. Most of this increase will be due to a scheduled $341.6 million increase in the earmark from the Michigan business tax to cover increased SAF payments to schools that will lose local property tax revenue due to the new personal property tax exemption.

YEAR-END BALANCE ESTIMATES

Based on the accounting of State revenue and expenditures as of December 18, 2007, the Senate Fiscal Agency (SFA) is estimating that the FY 2006-07 GF/GP budget will close the year with a balance of $242.3 million. The FY 2006-07 SAF budget will close the year with a balance of $76.2 million.

A comparison of the SFA's FY 2007-08 revenue estimate with enacted and projected appropriations leads to a $75.5 million GF/GP budget balance. The SFA is now estimating that the FY 2007-08 SAF budget is in balance by $58.5 million.

A review of the issues that the Governor and the Legislature will face in developing the FY 2008-09 State budget leads to the conclusion that both GF/GP and SAF appropriation growth will be restrained. This restrained level of FY 2008-09 appropriation growth results from continuing weak State revenue growth, coupled with spending pressures in several areas of the budget.

EXECUTIVE SUMMARY

SENATE FISCAL AGENCY
ECONOMIC AND BUDGET SUMMARY

ECONOMIC PROJECTIONS
(Calendar Year)

	2006 Actual	2007 Estimate	2008 Estimate	2009 Estimate
Real Gross Domestic Product (% change)	2.9%	2.2%	2.0%	2.8%
U.S. Consumer Price Index (% change)	3.2	2.7	3.2	2.8
Light Motor Vehicle Sales (millions of units)	16.5	16.0	15.8	16.3
U.S. Unemployment Rate (%)	4.6	4.5	4.9	5.1
Real Michigan Personal Income (% change)	0.2	1.8	(1.4)	0.4
Michigan Wage & Salary Employment (% change)	(1.1)	(1.4)	(1.9)	(0.9)

REVENUE ESTIMATES
GENERAL FUND/GENERAL PURPOSE (GF/GP) AND SCHOOL AID FUND (SAF)
(Millions of Dollars)

	FY 2007-08 Estimate			FY 2008-09 Estimate		
	Baseline	Tax Changes	Net Available	Baseline	Tax Changes	Net Available
Gen'l Fund/Gen'l Purpose	$8,089.5	$1,091.3	$9,180.8	$8,158.9	$966.4	$9,125.3
% Change	(2.6)%	---	10.4%	0.9%	---	(0.6)%
School Aid Fund	$11,155.9	$201.0	$11,357.1	$11,291.7	$587.7	$11,879.4
% Change	(0.2)%	---	1.8%	1.2%	---	4.6%
Total GF/GP and SAF	$19,245.4	$1,292.3	$20,537.9	$19,450.6	$1,554.1	$21,004.7
% Change	(1.2)%	---	5.5%	1.1%	---	2.3%

	FY 2007-08 Estimate	FY 2008-09 Estimate
Revenue Limit - Under (Over):	$5,015.7	$5,529.3

YEAR-END BALANCE ESTIMATES
(Fiscal Year, Millions of Dollars)

	FY 2006-07 Estimate	FY 2007-08 Estimate
General Fund/General Purpose	$242.3	$75.5
School Aid Fund	76.2	58.5
Budget Stabilization Fund	2.1	2.2

ECONOMIC REVIEW AND OUTLOOK

State revenue, particularly tax revenue, depends heavily on economic conditions. This section presents the Senate Fiscal Agency's latest economic forecast for 2008 and 2009, as well as a summary of recent economic activity and estimates for the rest of 2007.

RECENT ECONOMIC HIGHLIGHTS

In the aftermath of the 2001 recession, national wage and salary employment finally began increasing steadily in the second quarter of 2003. Between the second quarter of 2003 and the end of 2006, inflation-adjusted Gross Domestic Product (GDP) grew at a steady and generally healthy pace, averaging annual growth of 3.2%, and dipping below 2.1% only twice over the period. Much of this growth was fueled by high productivity and a strong housing market that largely offset the dragging effects of high and volatile energy prices, uncertainty resulting from various international political disputes, and restrained investment growth. The strong housing market enabled consumers to reduce saving and consume more even as employment growth was hampered by sustained productivity improvements and numerous energy price shocks.

During 2007, many of these factors lost their ability to overcome the drags on economic growth, or even became new drags on the economy, as in the case of the steep decline in housing markets. The slowdown has been reflected in lower levels of consumption, a substantial decline in residential investment spending, and weak business investment spending. Residential investment spending has fallen 16.3% over the last year and is down 23.5% from its peak in the fourth quarter of 2005. October housing starts were down 16.4% from the level a year earlier, and down 46.4% from the most recent cycle peak in January 2006. As the housing market has deteriorated and interest rates have risen, consumers have needed to adjust their behavior and consumption has suffered as a result. Details for selected economic indicators for the last few years are presented in Table 1 and Table 2.

The effect of high productivity on employment has been substantial since the 2001 recession. During the 1983-1989 and 1993-2000 recoveries, productivity increased by an average of approximately 2.0% per year, while wage and salary employment grew by an average of 2.6% per year. Those figures compare with a long-term average over the 1960-1992 period of annual productivity increases of 1.7% and employment gains of 2.2% per year. However, between 2001 and 2006, productivity averaged more than 2.6% per year and employment rose by only 0.65% per year. As overall productivity has declined in recent years, employment growth has strengthened. Wage and salary employment rose 1.1%, 1.7%, and 1.8% in 2004, 2005, and 2006, respectively; compared with average annual increases of 3.0% during 1983-1989 and 2.5% during 1993-2000.

Michigan's gains in personal income and employment have lagged behind the gains of nearly every other state in the country and occasionally trailed all of the states. The fact that Michigan has struggled so much compared with other states reflects the economic changes occurring in certain sectors of the economy combined with Michigan's industrial mix. Nationally, job losses during the recession were more severe, compared with the drop in inflation-adjusted GDP, than during previous recessions primarily because of substantial increases in productivity, particularly in the manufacturing sector. Similarly, job growth during the recovery has been slowed by continued high productivity. Although productivity growth slowed during 2006 and 2007 (Figure 1), it has continued to remain high in the durable goods manufacturing sector, a sector in which Michigan industry is disproportionately concentrated (Figure 2).

Table 1

THE SENATE FISCAL AGENCY ECONOMIC FORECAST (Calendar Years)	2005 Actual	2006 Actual	2007 Estimate	2008 Estimate	2009 Estimate
United States					
Nominal GDP					
(year-to-year growth)	6.4%	6.1%	4.9%	4.3%	5.8%
Inflation-Adjusted GDP					
(year-to-year growth)	3.1%	2.9%	2.2%	2.0%	2.8%
Unemployment Rate	5.1%	4.6%	4.5%	4.9%	5.1%
Inflation					
Consumer Price Index					
(year-to-year growth)	3.4%	3.2%	2.7%	3.2%	2.8%
GDP Implicit Price Deflator					
(year-to-year growth)	3.2%	3.2%	2.6%	2.2%	3.0%
Interest Rates					
90-day Treasury bill	3.15%	4.73%	4.57%	3.72%	4.40%
Corporate Aaa bond	5.23%	5.59%	5.65%	5.61%	5.99%
Federal funds rate	3.22%	4.97%	5.04%	4.34%	5.01%
Light Motor Vehicle Sales					
(millions of units)	16.9	16.5	16.0	15.8	16.3
Auto	7.7	7.8	7.5	7.4	7.6
Truck	9.3	8.7	8.5	8.4	8.7
Import Share	20.1%	22.4%	24.1%	24.8%	25.0%
Michigan					
Personal Income (millions)	$330,490	$341,075	$353,657	$357,199	$367,962
Year-to-year growth	3.7%	3.2%	3.7%	1.0%	3.0%
Inflation-Adjusted Personal Income (year-to-year growth)	0.7%	0.2%	1.8%	(1.4)%	0.4%
Wage & Salary Income (millions)	$183,652	$185,173	$190,054	$187,781	$190,988
Year-to-year growth	1.8%	0.8%	2.6%	(1.2)%	1.7%
Detroit Consumer Price Index					
(year-to-year growth)	2.9%	3.0%	1.9%	2.5%	2.6%
Wage & Salary Employment					
(thousands)	4,390.3	4,341.1	4,279.6	4,196.5	4,160.0
Year-to-year growth	(0.2)%	(1.1)%	(1.4)%	(1.9)%	(0.9)%
Unemployment Rate	6.8%	6.9%	7.2%	8.2%	8.5%

Table 2

THE SENATE FISCAL AGENCY U.S. ECONOMIC FORECAST DETAIL (Calendar Years)	2005 Actual	2006 Actual	2007 Estimate	2008 Estimate	2009 Estimate
Gross Domestic Product					
(billions of dollars)	$12,433.9	$13,194.7	$13,834.7	$14,432.1	$15,274.6
Year-to-year growth	6.4%	6.1%	4.9%	4.3%	5.8%
Inflation-Adjusted GDP and Components					
Gross Domestic Product					
(billions of 2000 dollars)	$11,003.4	$11,319.4	$11,569.0	$11,803.9	$12,129.1
Year-to-year growth	3.1%	2.9%	2.2%	2.0%	2.8%
Consumption					
(billions of 2000 dollars)	$7,803.6	$8,044.1	$8,275.3	$8,425.1	$8,636.0
Year-to-year growth	3.2%	3.1%	2.9%	1.8%	2.5%
Business Fixed Investment					
(billions of 2000 dollars)	$1,225.8	$1,306.8	$1,368.6	$1,439.7	$1,501.0
Year-to-year growth	7.1%	6.6%	4.7%	5.2%	4.3%
Change in Business Inventories					
(billions of 2000 dollars)	$33.2	$40.3	$10.6	$11.6	$20.7
Residential Investment					
(billions of 2000 dollars)	$597.1	$569.5	$470.7	$348.3	$361.0
Year-to-year growth	6.6%	-4.6%	-17.3%	-26.0%	3.6%
Government Spending					
(billions of 2000 dollars)	$1,946.3	$1,981.4	$2,021.5	$2,060.4	$2,072.5
Year-to-year growth	0.8%	1.8%	2.0%	1.9%	0.6%
Net Exports					
(billions of 2000 dollars)	($618.1)	($624.5)	($554.2)	($430.2)	($399.0)
Exports (billions of 2000 dollars)	$1,203.4	$1,304.1	$1,416.2	$1,592.2	$1,718.2
Imports (billions of 2000 dollars)	$1,821.5	$1,928.6	$1,970.4	$2,022.4	$2,117.1
Personal Income					
(year-to-year growth)	5.9%	6.6%	6.6%	5.1%	5.4%
Adjusted for Inflation	2.4%	3.3%	3.8%	1.9%	2.5%
Wage & Salary Income					
(year-to-year growth)	5.1%	6.2%	6.6%	5.0%	5.3%
Personal Savings Rate	0.5%	0.4%	0.8%	1.0%	1.4%
Capacity Utilization Rate	80.2%	81.7%	81.7%	81.2%	81.7%
Housing Starts (millions of units)	2.068	1.801	1.331	0.827	0.986
Conventional Mortgage Rates	5.9%	6.4%	6.5%	6.3%	6.5%
Federal Budget Surplus					
(billions of dollars, NIPA basis)	($318.3)	($220.0)	($174.2)	($192.7)	($204.6)

Productivity gains provide a number of positive economic benefits, including lower product prices and greater income growth in the future. However, productivity offers a transitory negative economic effect with its impact on job growth. For example, with stable sales, an 8.0% increase in productivity in one year (such as experienced in durable goods manufacturing over the 2002-2003 period) means that a firm could reduce its labor force by 8.0% that year and still produce the output needed to meet demand. In the case of Michigan's largest industry -- transportation equipment manufacturing -- total sales of light vehicles have remained fairly flat while vehicle sales of the domestic manufacturers (primarily DaimlerChrysler, Ford, and General Motors) have comprised a decreasing share of total sales (from 68.1% in 2000 to 56.5% in 2006, and 52.4% through November 2007).

Figure 1

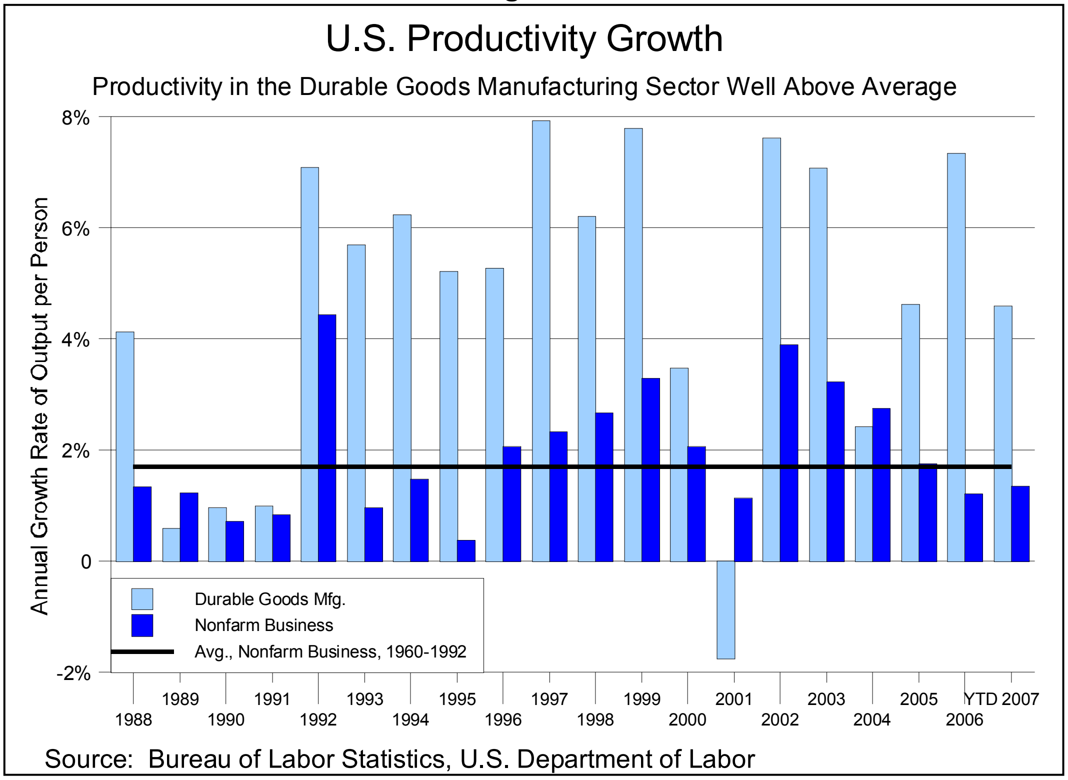
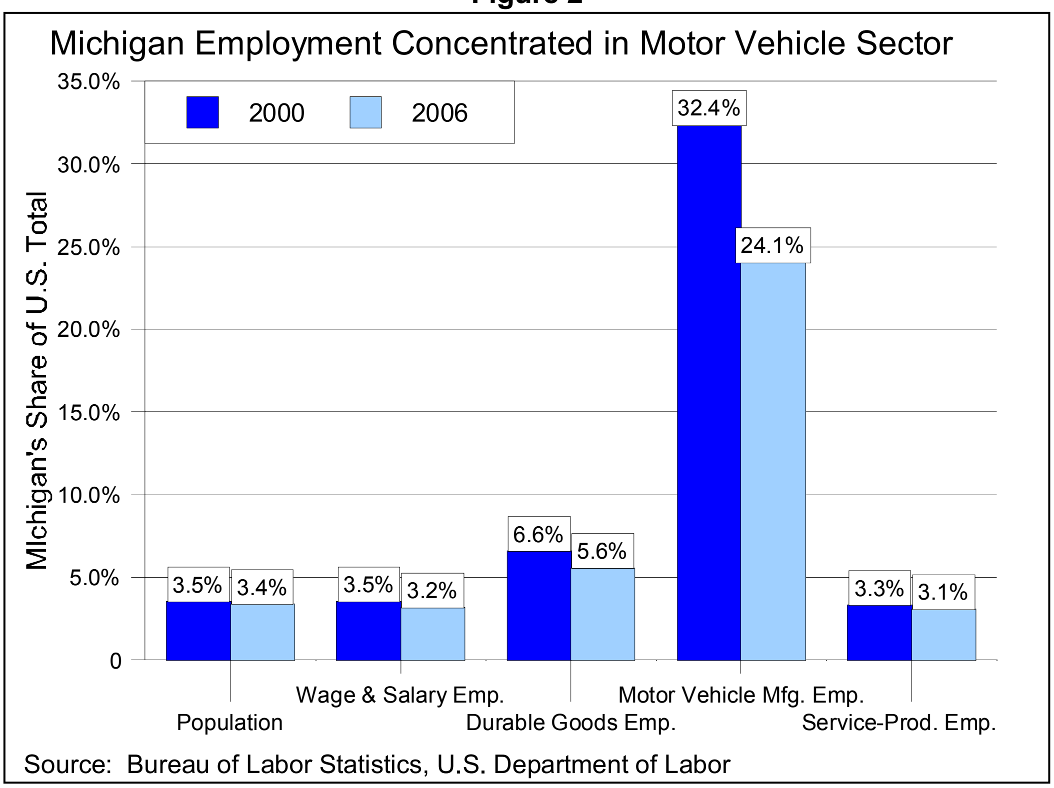


Figure 2



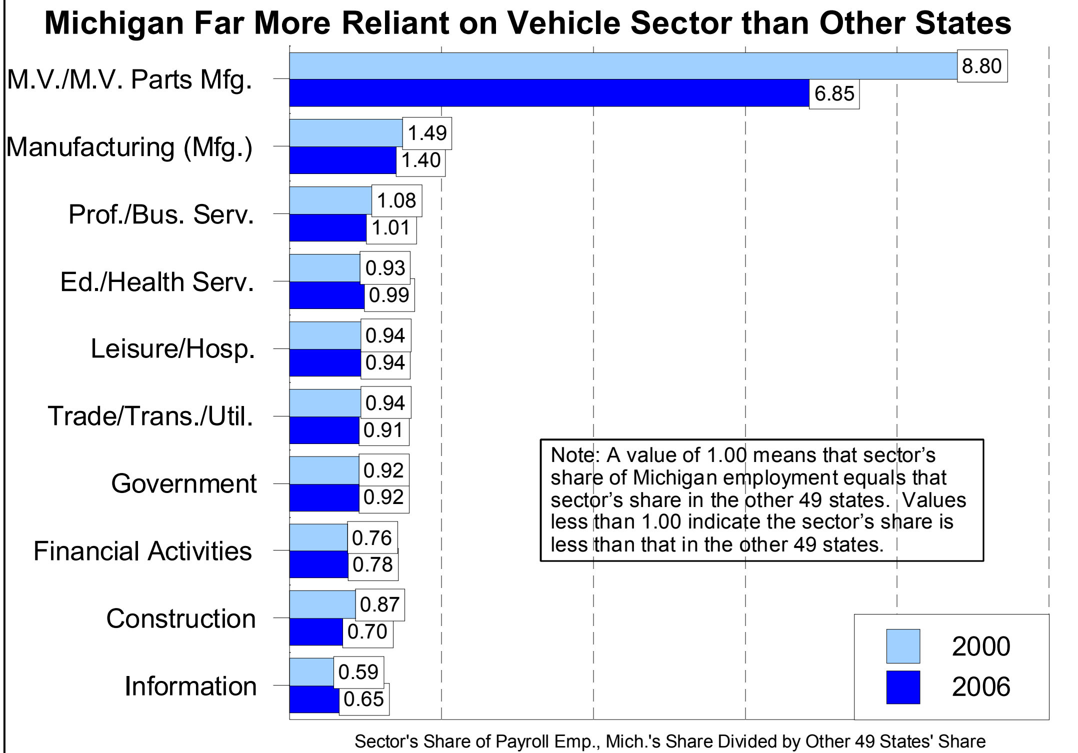
As indicated earlier, productivity has risen most significantly in economic sectors in which the Michigan economy is heavily concentrated. Sales for those industries have remained mostly flat or slightly down, while Michigan's share of the market has declined markedly. Even after six years of employment declines, especially within those areas where Michigan is most concentrated relative to other states, Michigan is still heavily dependent upon sectors that are highly cyclical and likely to continue to experience substantial gains in productivity and declines in employment. Based on data through 2006, Michigan represented 3.2% of the national economy, yet comprised 4.6% of manufacturing goods employment and 5.6% of durable goods manufacturing employment. Transportation equipment manufacturing comprises approximately 43.3% of Michigan's durable goods manufacturing employment and Michigan's motor vehicle manufacturing employment comprises nearly one-fourth of the nation's motor vehicle manufacturing employment.

Another way to see how concentrated Michigan is on motor vehicle manufacturing is to examine the share of total employment related to motor vehicle production. Employment in motor vehicle manufacturing and motor vehicle parts manufacturing comprised 6.9% of Michigan employment in 2000, before the current contraction in motor vehicle-related manufacturing employment, and 4.7% in 2006. However, after Michigan, the state next most reliant on motor vehicle-related manufacturing is Indiana, where that sector represented 3.5% of total employment in 2000 and 2.9% in 2006. Compared with the national average, where the sector comprised 0.6% of employment in 2000 and 0.5% in 2006, Michigan was 8.8 times more concentrated in motor vehicle-related employment than the rest of the nation as a whole in 2000 and was still more than 6.9 times as concentrated in 2006 (Figure 3). These measures exclude other sectors in those states, such as the fabricated metals manufacturing sector, that may be heavily reliant on sales to vehicle manufacturers located within the state. Furthermore, 38 states have either negligible or no motor vehicle manufacturing-related employment.

While more difficult to quantify, many of Michigan's nonmanufacturing sectors rely heavily, either directly or indirectly, on activity in the motor vehicle sector. Average wages in transportation equipment manufacturing are higher than in any other economic sector in Michigan, and those workers purchase goods and services across the spectrum for their own consumption. In addition, vehicle manufacturers are significant consumers of a variety of goods and services as well. In 2006, wages and salaries paid to workers in the motor vehicle manufacturing sector comprised 1.2% of private sector wages and salaries paid nationally, but 10.1% of wages and salaries paid in Michigan (Figure 4). As a result, economic downturns (from either declining employment or falling business profits) in the motor vehicle sector are transmitted and multiplied throughout the Michigan economy, just as any national or local economic shock is transmitted through the affected economies, but will have a greater proportional impact on Michigan than on any other state or the nation as a whole (Figure 5).

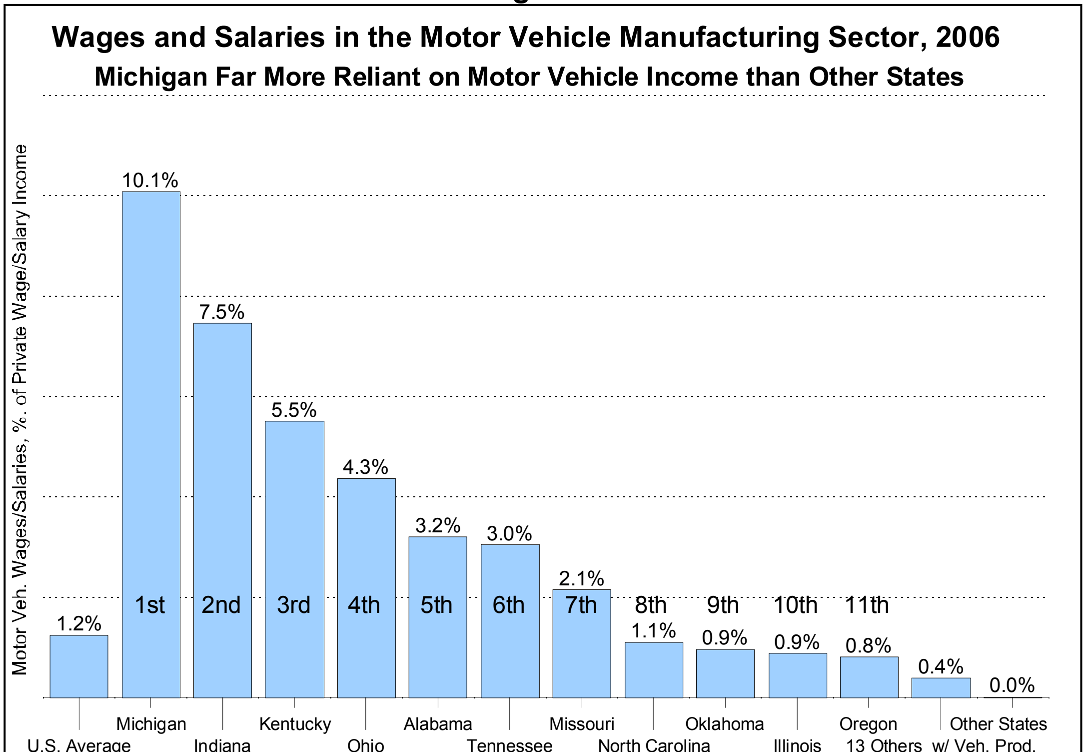
Many of the factors affecting job growth over the last few years are expected to continue to influence the economy over the forecast period. The principal factors affecting the economy, and which present risks to the forecast, are: 1) weakness in the housing market, and how it will influence both consumer behavior and credit market liquidity; and 2) inflationary pressures, particularly from wage pressures, energy and commodity prices, changes in productivity, and depreciation of the U.S. dollar.

Figure 3



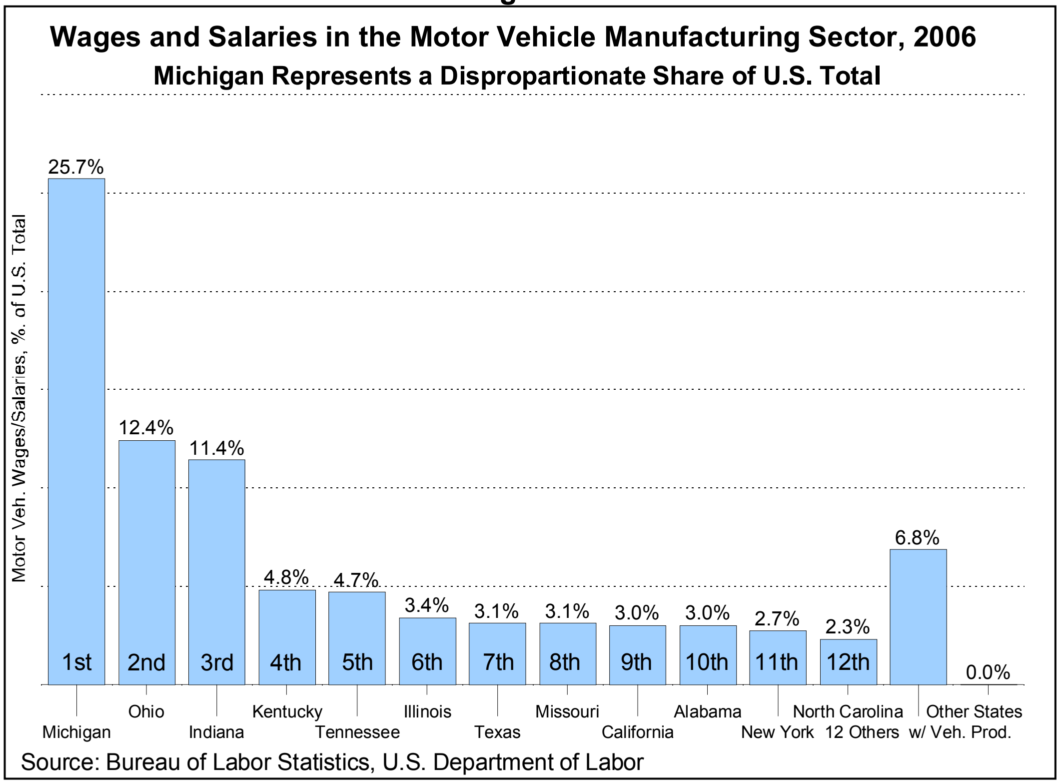
Source: Bureau of Labor Statistics, U.S. Department of Labor

Figure 4



Source: Bureau of Labor Statistics, U.S. Department of Labor

Figure 5

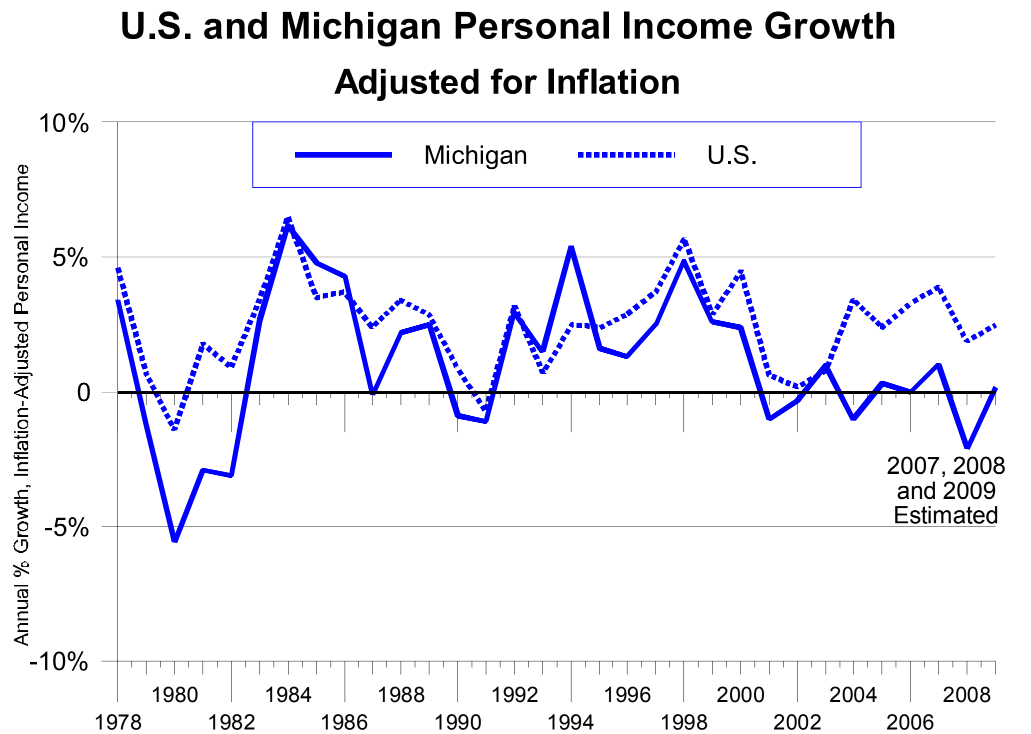


FORECAST SUMMARY

The U.S. economy is expected to continue growing over the forecast period, although some quarters during the next year will near recession levels, while the Michigan economy will essentially be in recession over the forecast period. Table 1 and Table 2 provide a summary of key economic indicators from the SFA's economic forecast, with references to recent years. Inflation-adjusted GDP is projected to grow 2.2% in 2007, but only 2.0% in 2008 before growing 2.8% in 2009. The decline in growth during 2008 primarily reflects lower residential investment and much weaker consumption growth. The U.S. unemployment rate is expected to increase, from 4.5% during 2007 to 4.9% in 2008 and 5.1% in 2009.

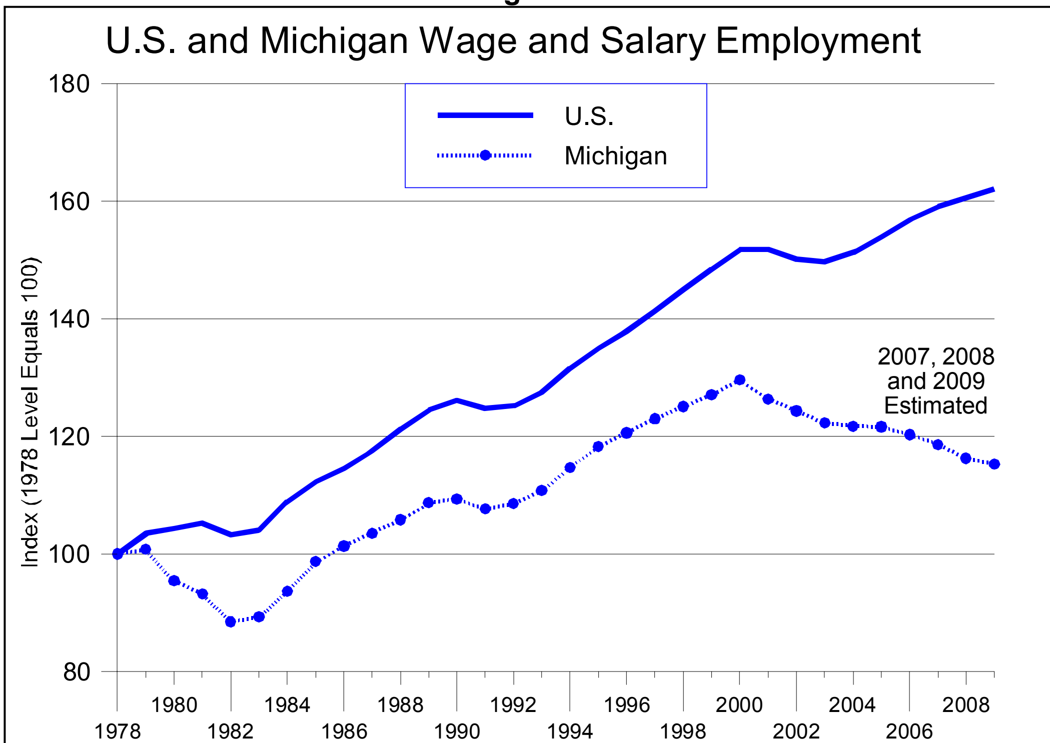
In Michigan, both job growth and personal income growth are expected to remain below the national average and the historical State average (Figures 6 and 7) and spend most of the forecast period in recession. Inflation-adjusted personal income is forecasted to rise 1.8% in 2007, but will decline 1.4% in 2008 and only rise 0.4% in 2009. Wage and salary employment is projected to fall 1.4% in 2007 and 1.9% in 2008. The rate of employment declines should begin tapering during 2009 although employment is still forecast to decline 0.9% (Table 1). The declines in wage and salary employment will extend the period of employment declines to nine consecutive years, the longest period on record. These declines will largely reflect continued high productivity and competitive pressures, particularly in the manufacturing sector. Nationally, light vehicle sales are expected to decline slightly, to 16.0 million units in 2007 and 15.8 million units in 2008, before rising to 16.3 million units in 2009. Declining vehicle sales, combined with productivity improvements and declining market share for domestic vehicle manufacturers, will depress employment and labor force participation. In Michigan, as a result, the unemployment rate will increase from 7.2% in 2007 to 8.2% in 2008 and 8.5% in 2009, keeping the Michigan unemployment rate well above the national average.

Figure 6



Source: U.S. Department of Commerce and the Senate Fiscal Agency

Figure 7



Source: U.S. Department of Labor and the Senate Fiscal Agency

Compared with the May 18, 2007, consensus economic forecast, both the U.S. and Michigan forecasts for 2008 are considerably weaker, while the changes in the Michigan forecast for 2007 are mixed. For 2007, the Michigan forecast projects stronger income growth but weaker employment growth than was forecast in May. Inflation measures are expected to rise somewhat more rapidly than was predicted in May.

FORECAST ASSUMPTIONS

Forecasting the behavior of the economy requires making assumptions about the behavior of certain key economic variables. The current SFA forecast for 2008 and 2009 is based upon the following assumptions:

Monetary Policy. The Federal funds rate target is currently 4.25%, down 100 basis points from May 2007. The reduction in the rate was not expected in the May 2007 Consensus estimate and reflects the Federal Reserve Board's concerns regarding liquidity constraints arising from the slowdown in the housing market. However, the statements issued with these announced rate reductions have continued to focus on significant inflationary concerns. The forecast assumes that a number of inflationary concerns are realized to some degree and that the Federal Reserve Board will act to keep inflation in check, even at the expense of slowing down an already sluggish economy. As a result, interest rates are anticipated to remain steady through most of 2008, with the Federal funds rate remaining at 4.25% before beginning to rise in late 2008 and reaching 4.75% by early 2009 and 5.50% by the end of 2009.

Foreign Economies. Many of the U.S.'s key trading partners' economies are expected to grow more rapidly than the U.S. economy during 2008 and most of 2009. After an expected decline of 4.7% during 2007, the U.S. dollar is expected to fall in value another 8.2% during 2008 and 3.1% during 2009. As a result, the forecast predicts that the trade deficit will decrease, shrinking from about 5.5% of GDP during 2006 to approximately 3.3% during 2009.

Oil and Energy Prices. The forecast expects oil prices in 2007 and 2008 to remain stable, and well above even recent historical averages, with the price of West Texas intermediate crude above $85 per barrel through virtually all of the forecast horizon. Other energy prices are expected to rise moderately over the forecast period. Prices are expected to remain above historical averages for a variety of reasons, ranging from political instability in many oil-producing nations to limited domestic refining capacity (which is essentially already at maximum) to growing domestic and worldwide energy demands.

RISKS TO THE FORECAST

All forecasts carry a certain amount of error, but the chances that a forecast will err substantially depend upon certain risks to economic fundamentals upon which the forecast is built. While recent years have offered a fair amount of economic uncertainty, the economic environment in 2008 exhibits even greater uncertainty, with many indicators suggesting a recession is possible or even likely during the year. While the current forecast does not expect the U.S. economy to experience a recession during the forecast horizon, growth is expected to be weak. As a result, the current economic forecast faces a number of risks, most suggesting that in inflation-adjusted terms, the economy could be weaker than forecasted or even recessionary.

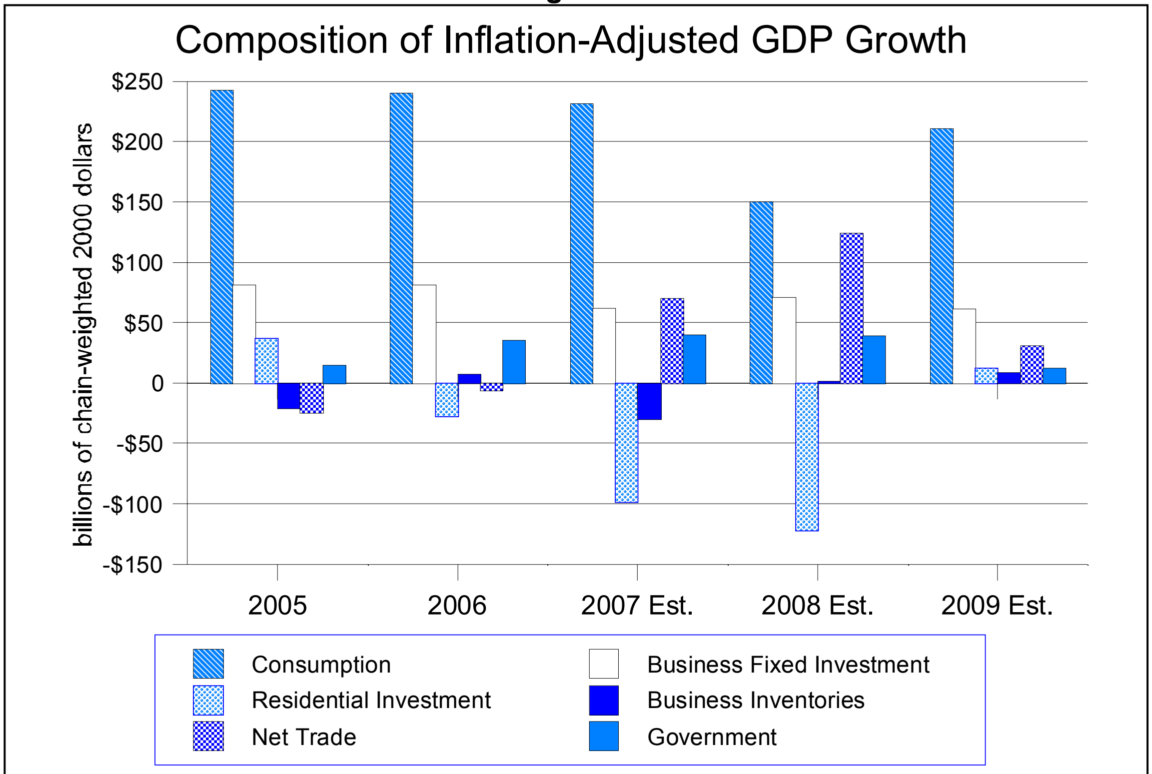
Consumer Behavior. Consumption growth remained moderate throughout the slow recovery during the first part of the decade, largely through increased borrowing and housing refinance activity. Households generally felt wealthier, despite flat or declining inflation-adjusted wages, because the stock market was improving and home values were soaring. However, higher interest rates have worsened the burden of servicing consumer debt and weaker expectations for consumption are already lowering business plans for investment for much of the forecast period. The burden of servicing consumer debt reached an all-time high in the fourth quarter of 2006 and has remained near that level. A significant portion of debt is variable-rate debt -- meaning that the burden will increase if interest rates rise more quickly than income. When combined with slow job growth, continued high energy prices, a declining value of the dollar, and modest personal income growth, consumption growth is not likely to rise significantly over the forecast period. Weak financial markets and declining housing prices are likely to provide significant incentives for consumers to increase the personal saving rate from its current negative levels, although the rate will remain near record lows if predicted consumption levels are generally correct. If the saving rate improves more than expected and/or higher interest rates have a greater effect than forecasted, both consumption growth and economic growth will be lower. Similarly, if the weak employment situation causes consumers to lose confidence in the economy, consumer spending (and thus economic growth) may be lower than expected.

Inflation. While the forecast expects the rate of inflation to be only slightly higher in 2008 and 2009, compared with 2007, a significant number of economic factors suggest that inflation could be a more significant issue. The assumption of largely stable energy prices has implications for both consumers and businesses: higher energy expenses tend to create uncertainty in the economy, consumers often divert consumption from other areas to support the higher cost of energy, and businesses find it more costly to operate. With the petroleum refining sector operating at nearly 100% capacity, global energy demand rising, and oil production somewhat strained in the near future, energy prices may be substantially greater than forecasted even without external shocks. Additionally, the dollar's value is expected to decline, increasing the price of imports and giving greater pricing power to domestic producers, particularly those needing to pass on higher energy prices. Producers are likely also to face wage pressures that will be compounded by the fact that productivity, while still exhibiting historically strong growth, is growing more slowly than in recent years. Additionally, productivity in nonmanufacturing sectors has shown a marked slowdown in recent quarters, adding to the cost pressures producers are experiencing.

Inflation is largely held down in the forecast by a slower economy: moderate growth in productivity, which may not be as strong as forecasted; minimal wage growth, which may be stronger than predicted; and moderate declines in the value of the dollar, which may fall in value more rapidly than expected. Furthermore, the Federal Reserve Board is assumed to maintain a successfully proactive approach to inflationary pressures.

The International Economy. The current forecast does not expect a recession in the U.S. economy during 2008. However, the lack of a recession owes perhaps even more to the assumptions for export growth than to the assumptions regarding consumer behavior. The declines in the value of the dollar will make U.S. exports more attractive to other nations and raise the cost of imports in the United States. Economic growth in the U.S.'s major trading partners is assumed to remain solid. As a result, more than 50.0% of the net economic growth experienced in 2008 will be due to the improvement in net trade (Figure 8). There is a substantial chance that foreign growth will be slower than forecast and thus trade will not contribute as much toward U.S. economic growth. Furthermore, under such a scenario, the economy still would experience all of the inflationary pressures of currency devaluation, but without the accompanying acceleration in exports. There is a small chance that the value of the dollar will decline less than expected, which again would lower growth from the trade sector but would produce less inflationary pressure. As a result, virtually all of the risk for the forecast regarding trade is on the side for lower economic growth.

Figure 8



Source: U.S. Department of Commerce and the Senate Fiscal Agency

Michigan's Situation. Michigan's economic performance over the last seven years is actually consistent with what has happened in other states, despite Michigan's employment situation ranking at or among the lowest in the nation (Figure 9). Generally, states with higher manufacturing concentrations (particularly in the transportation equipment manufacturing sector) have experienced weaker job performance over the last seven years, both because of the economic changes occurring in that sector and because of the dependence of other sectors within those states on manufacturing activity. As indicated earlier, productivity gains have made American manufacturing firms more profitable and more competitive, but have reduced the need for hiring additional employees to meet increased demand.

Weak markets for housing, credit, and employment, high energy prices, and substantial debt burdens are expected to exert a dragging force on any increases in demand over the forecast period. U.S. vehicle sales are expected to drop below 16.0 million units for the first time in a decade, while the domestic share of the sales mix is expected to continue declining. Michigan's economic fortunes historically have been very closely linked with sales of domestically produced light vehicles (Figure 10), so it is unclear whether Michigan's employment situation would be much better even if productivity were not rising so rapidly in the motor vehicle sector. However, the combination of high productivity and declining market share has been particularly dramatic: On a seasonally adjusted basis, as of October 2007, Michigan had lost approximately one-half of the jobs (46.0%, a decline of more than 163,000 jobs) in transportation equipment manufacturing that existed during the peak in July 2000.

Figure 9

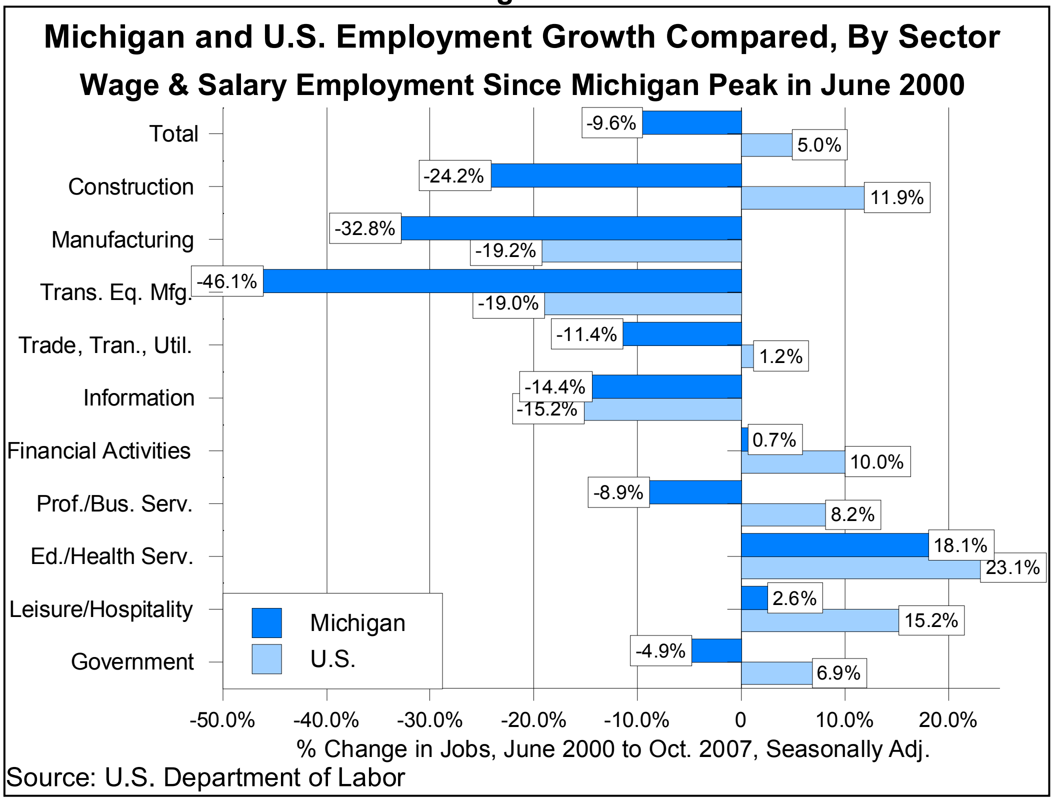
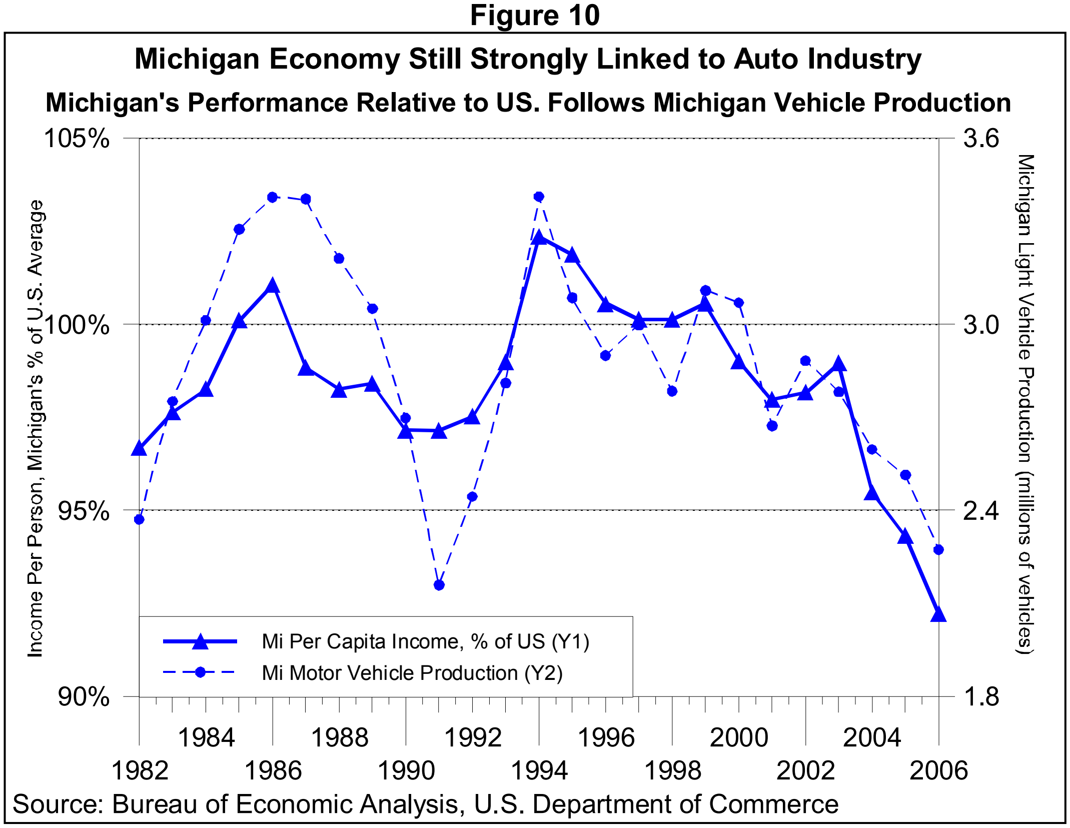


Figure 10



Complicating the economic landscape, much of the downsizing in the domestic transportation equipment manufacturing sector actually has led auto companies to close facilities in other states more often than in Michigan. While those states were already less reliant on transportation equipment manufacturing, the changes have made them even less dependent. However, this "retreat-to-the-core" strategy means that Michigan's economy has become less reliant on transportation equipment manufacturing at a slower rate than in the rest of the country. As a result, while that strategy has preserved more transportation equipment manufacturing jobs in Michigan than might otherwise have been saved, it means that the Michigan economy is more likely than other states to remain far more vulnerable to swings in the domestic vehicle manufacturing industry.

Because of the number of individuals employed in transportation equipment manufacturing and the likelihood of continued substantial gains in productivity in the vehicle sector, it is likely that absent any shocks, the Michigan economy will spend years adjusting to the change. Offsetting a 10.0% annual decline in employment in the transportation equipment manufacturing sector essentially requires nearly 0.7% annual employment growth in the rest of the Michigan economy. Between 1995 and 2000, overall employment in Michigan grew only an average of 1.8% per year (and transportation equipment manufacturing employment over that period increased an average of 1.4% per year). For overall employment in Michigan to rise 1.8%, despite a 10.0% decline in transportation equipment manufacturing employment, employment in the rest of the Michigan economy would need rise by more than 2.5%, which has occurred only in three years since 1986 (and only in six of the last 25 years). Given that productivity improvements, changes in market share, and changing demographics are likely to result in a decline in transportation equipment manufacturing employment of 10.0% or more a year over a number of future years, if employment in other sectors grows at the 1990-2004 average of 0.9% per year, Michigan will not reach the 2000 level of employment again until some time after the year 2026.

The dilemma for Michigan is that for the economy and tax revenue to improve, employment gains need to occur. However, given Michigan's reliance on the automobile industry and manufacturing and the forecast for both vehicle sales and overall consumption, employment gains are likely to occur only if productivity growth declines. On the other hand, lower productivity growth will impede the ability of Michigan businesses to compete and to be profitable. Therefore, Michigan is put in the dilemma that if productivity improves, there will be very little pressure to create additional jobs, although Michigan businesses will be better able to thrive; while if productivity growth falls, there will be a short-term improvement in employment that is likely to be lost as Michigan businesses find it more difficult to compete in the market with firms that are enjoying productivity improvements.

For Michigan, the biggest risks to the forecast are that vehicle sales are less than forecasted, that market shares for Michigan-based vehicle manufacturers fall more rapidly than predicted, that Michigan vehicle production is reduced more rapidly and/or by greater amounts than expected, and that the economic slowdown at the national level takes a greater toll on the consumption of nonvehicle-related goods and services provided by Michigan. For eight years, the fundamental changes occurring in manufacturing across the globe combined with falling market shares for Michigan manufacturers have kept the State in an employment recession. The depth and duration of Michigan's employment recession will depend upon the strength of those markets and how rapidly Michigan producers transform their businesses. That transformation process will inevitably involve job losses. The more rapidly the transformation occurs, and/or the slower the national and international economies, the steeper the decline in Michigan employment will be in the near term. However, a more rapid transformation also would allow Michigan to emerge from its employment recessions more quickly.

THE FORECAST FOR STATE REVENUE

This section presents the Senate Fiscal Agency's (SFA's) estimates for General Fund/General Purpose (GF/GP) and School Aid Fund (SAF) revenue. The preliminary year-end revenue for FY 2006-07 is presented along with the revised estimates for FY 2007-08 and the initial revenue estimates for FY 2008-09. The revenue estimates for each of these fiscal years include the estimates for baseline revenue, which measures what the revenue would be without any changes in the State's tax structure, and net revenue, which equals baseline revenue adjusted for the impact of all enacted tax changes. In addition, this revenue represents the revenue generated from ongoing revenue sources and does not include the revenue generated each year through one-time revenue transfers and other revenue adjustments. The one-time revenue used to balance the GF/GP and SAF budgets in FY 2006-07 and FY 2007-08 is discussed in the last section of this report.

REVENUE OVERVIEW

In FY 2006-07, GF/GP and SAF revenue totaled $19.47 billion. The bad news is that this represents a very modest gain of only 0.6% from the FY 2005-06 level, but the good news is that revenue in FY 2006-07 came in stronger than was expected. The consensus revenue estimate adopted in May 2007 projected that GF/GP and SAF revenue would decline by a slight 0.4% in FY 2006-07. Revenue was stronger than expected due in large part to increases in income tax withholding revenue. While wage and salary employment continued to trend down during FY 2006-07, average earnings per worker were up more than was expected and this helped bolster income tax payments. Collections also edged up for the State education, casino, liquor, beer, and wine taxes, but these gains were largely offset by declines in the sales, single business, and real estate transfer taxes. On a baseline basis, GF/GP and SAF revenue collections were up 1.2% in FY 2006-07.

As presented in the first section of this report, Michigan's economic activity is expected to slow further in 2008 before rebounding modestly in 2009. As a result, baseline GF/GP and SAF revenue is expected to decline 1.2% in FY 2007-08; however, recently enacted major tax increases will help boost GF/GP and SAF revenue 5.5% in FY 2007-08 to $20.54 billion. These tax increases include an increase in the income tax rate and the replacement of the single business with the Michigan business tax. When originally adopted in July 2007, the switch to the Michigan business tax was designed to be revenue neutral with the outgoing single business tax; however, in October a surcharge was attached to this new business tax to help balance the budget for FY 2007-08 (by replacing an enacted expansion of the use tax to certain services) and help eliminate the State's structural budget imbalance on an ongoing basis.

In FY 2008-09, GF/GP and SAF revenue will total an estimated $21.0 billion, which represents a 2.3% increase from the revised estimate for FY 2007-08. One of the major reasons for the expected increase in GF/GP and SAF revenue in FY 2008-09 is modest improvement in the level of economic activity, which will help boost baseline revenue growth to 1.1%. The revenue estimates for FY 2007-08 and FY 2008-09 are summarized in Table 3.

Table 3

SENATE FISCAL AGENCY REVENUE ESTIMATES FOR FY 2007-08 AND FY 2008-09
GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND
(Millions of Dollars)

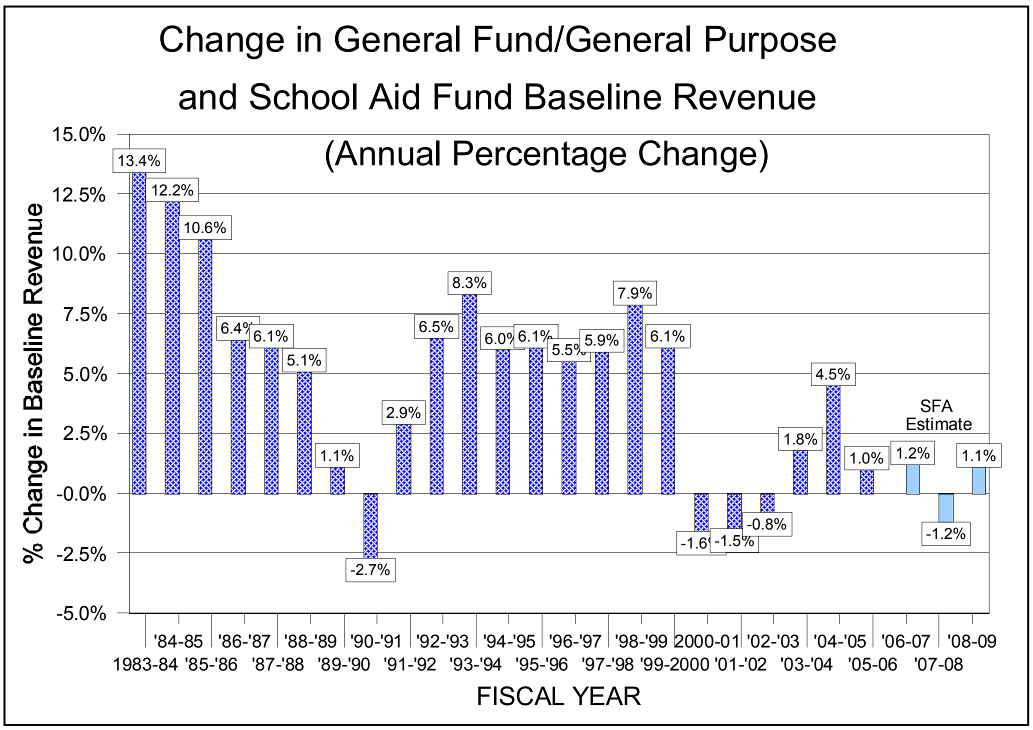
	FY 2006-07 Preliminary Final	FY 2007-08 Revised Estimate	FY 2008-09 Initial Estimate
GENERAL FUND/GENERAL PURPOSE			
Baseline Revenue	$8,306.2	$8,089.5	$8,158.9
Tax Changes Not In Baseline	11.4	1,091.3	966.4
Revenue After Tax Changes:			
Net Income Tax	4,330.4	4,957.7	4,894.9
SBT, Michigan Business Tax, & Insurance Tax	2,039.9	2,353.8	2,365.2
Other Taxes	1,574.3	1,519.6	1,519.6
Total Taxes	7,944.5	8,831.2	8,779.7
Nontax Revenue	373.0	349.6	345.6
TOTAL GF/GP REVENUE[1)]	**$8,317.6**	**$9,180.8**	**$9,125.3**
SCHOOL AID FUND			
Baseline SAF	$11,179.3	$11,155.9	$11,291.7
Tax Changes Not In Baseline	(26.0)	201.0	587.7
TOTAL SAF REVENUE	**$11,153.3**	**$11,357.1**	**$11,879.4**
BASELINE GF/GP & SAF REVENUE	19,485.6	19,245.4	19,450.6
Tax & Revenue Changes	(14.6)	1,292.3	1,554.1
GF/GP & SAF REV. AFTER CHANGES	**$19,471.0**	**$20,537.8**	**$21,004.7**
ADDENDUM:			
Sales Tax	$6,552.2	$6,511.3	$6,552.1
		PERCENT CHANGE	
GENERAL FUND/GENERAL PURPOSE			
Baseline Revenue	1.8%	(2.6)%	0.9%
Revenue After Tax Changes:			
Net Income Tax	4.0	14.5	(1.3)
Single Business Tax & Insurance Tax	(1.4)	15.4	0.5
Other Taxes	(7.6)	(3.5)	(0.0)
Total Taxes	7.5	11.2	(0.6)
Nontax Revenue	12.7	(6.3)	(1.1)
TOTAL GF/GP REVENUE	**0.6%**	**10.4%**	**(0.6)%**
SCHOOL AID FUND			
Baseline SAF	0.7	(0.2)	1.2
TOTAL SAF REVENUE	**0.6%**	**1.8%**	**4.6%**
BASELINE GF/GP & SAF REVENUE	1.2	(1.2)	1.1
GF/GP & SAF REV. AFTER CHANGES	**0.6%**	**5.5%**	**2.3%**
ADDENDUM:			
Sales Tax	(1.3)%	(0.6)%	0.6%

1) The single business tax (SBT) will be replaced with the Michigan business tax (MBT) effective January 1, 2008. As a result, FY 2007-08 includes revenue from both the SBT and the MBT and FY 2008-09 includes revenue only from the MBT.

Historical Perspective

Figure 11 presents a historical overview of the percentage change in baseline GF/GP and SAF revenue since FY 1983-84, and helps illustrate the dramatic deterioration that has occurred in the annual rate of growth since FY 1999-2000. From FY 1992-93 to FY 1999-2000, baseline revenue growth averaged 6.5% and did not fall below 5.5% during these eight years. This remarkable period of fairly strong, consistent revenue growth came to an abrupt end as the recession hit Michigan in the second half of 2000 and baseline revenue actually declined for three consecutive years, from FY 2000-01 to FY 2001-02. Revenue growth finally turned positive again in FY 2003-04 with a gain of 1.8% and then it increased 4.5% in FY 2004-05. This increase in the pace of revenue growth was short-lived, however, as baseline revenue growth fell back to 1.0% in FY 2005-06 and to 1.2%, in FY 2006-07. In FY 2007-08, baseline GF/GP and SAF revenue is expected to decline 1.2%, which would make it similar to the declines experienced in FY 2000-01 through FY 2002-03. While the rate of growth is expected to rebound in FY 2008-09 to a 1.1% increase, this will still be well below the rates of growth experienced during most of the 1990s.

Figure 11



FY 2006-07 PRELIMINARY YEAR-END REVENUE

Based on preliminary year-end book-closing revenue data, GF/GP and SAF revenue from ongoing revenue sources totaled $19.47 billion in FY 2006-07, which was up 0.6% from the FY 2005-06 revenue level, as presented in Table 4. Tax and nontax revenue collections were stronger than expected as the preliminary year-end revenue level for FY 2006-07 is up $206.3 million from the consensus estimate adopted at the May 2007 Consensus Revenue Estimating Conference.

Table 4

FY 2006-07 PRELIMINARY FINAL REVENUE GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND (Millions of Dollars)					
			Change from FY 2005-06		
	FY 2005-06 Final	FY 2006-07 Preliminary Final	Dollar Change	Percent Change	$ Change from 05/07 Consensus
GENERAL FUND/GENERAL PURPOSE:					
Baseline Revenue	$8,156.6	$8,306.2	$149.6	1.8%	$102.5
Tax Changes Not In Baseline	109.5	11.4	(98.0)	---	(0.7)
Revenue After Tax Changes					
Personal Income Tax					
Gross Collections	7,849.9	8,129.5	279.6	3.6	91.7
Less: Refunds	(1,625.7)	(1,687.3)	(61.6)	3.8	13.4
Net Income Tax Collections	6,224.2	6,442.2	218.0	3.5	105.1
Less: Earmarking to SAF	(2,038.9)	(2,110.3)	(71.5)	3.5	(24.7)
Campaign Fund	(1.3)	(1.5)	(0.2)	15.4	0.0
Net Income Tax to GF/GP	4,184.0	4,330.4	146.3	3.5	80.4
Other Taxes					
Single Business Tax	1,841.9	1,816.1	(25.8)	(1.4)	5.8
Sales	85.9	83.1	(2.8)	(3.3)	(0.3)
Use	917.0	920.0	3.0	0.3	(9.7)
Cigarette	229.0	225.4	(3.6)	(1.6)	(1.7)
Insurance Company Premiums	219.5	223.8	4.3	2.0	7.8
Telephone & Telegraph	83.5	87.3	3.8	4.6	9.3
Estate	0.6	0.7	0.1	16.7	0.7
Oil & Gas Severance	81.5	72.0	(9.5)	(11.7)	10.0
Casino Wagering	45.0	46.1	1.1	---	---
All Other	128.6	139.7	11.1	8.6	(2.5)
Subtotal Other Taxes	3,632.5	3,614.2	(18.3)	(0.5)	18.5
Total Nontax Revenue	449.6	373.0	(76.6)	(17.0)	31.1
GF/GP REV. AFTER TAX CHANGES	**$8,266.1**	**$8,317.6**	**$51.6**	**0.6%**	**$130.2**
SCHOOL AID FUND:					
Baseline Revenue	$11,106.6	$11,179.3	$72.7	0.7%	$97.9
Tax Changes Not In Baseline	(24.6)	(26.0)	(1.4)	5.8	(21.7)
Revenue After Tax Changes					
Sales Tax	4,831.3	4,768.5	(62.8)	(1.3)	(7.3)
Lottery Revenue	688.0	748.9	60.9	8.9	38.9
State Education Property Tax	2,003.5	2,081.0	77.5	3.9	11.9
Real Estate Transfer Tax	297.7	237.5	(60.2)	(20.2)	11.3
Income Tax	2,038.9	2,110.3	71.5	3.5	24.7
Casino Tax	104.1	106.7	2.6	2.5	(2.4)
Other Revenue	1,118.6	1,100.3	(18.2)	(1.6)	(0.8)
SAF REV. AFTER TAX CHANGES	**$11,082.0**	**$11,153.3**	**$71.3**	**0.6%**	**$76.2**
BASELINE GF/GP AND SAF	$19,263.3	$19,485.6	$222.3	1.2%	$200.4
Tax & Revenue Changes	84.9	(14.6)	(99.5)	---	5.9
GF/GP & SAF REV. AFTER CHANGES	**$19,348.1**	**$19,471.0**	**$122.8**	**0.6%**	**$206.3**
SALES TAX	$6,638.1	$6,552.2	$(85.9)	(1.3)%	$(10.1)
Note: FY 2006-07 is the base year for baseline revenue.					

General Fund/General Purpose

General Fund/General Purpose revenue totaled $8.32 billion in FY 2006-07, which was up 0.6% from FY 2005-06. This preliminary year-end revenue level is $130.2 million above the May 2007 consensus revenue estimate. The increase from the May estimate was primarily due to stronger-than-expected increases in income tax collections and nontax revenue sources including the profit from the State's liquor sales. This GF/GP revenue from ongoing taxes and nontax sources does not include the roughly $930.0 million included in the GF/GP budget for FY 2006-07 from one-time sources. This one-time revenue is discussed in the last section of this report. A breakdown of FY 2006-07 GF/GP revenue is presented in Table 4.

School Aid Fund

The tax and lottery revenue earmarked to the SAF totaled $11.15 billion in FY 2006-07, which was up 0.6% from the FY 2005-06 revenue level. Revenue from the income, State education, and casino taxes was up in FY 2006-07, as was the net revenue from the lottery. These gains were, however, partially offset by declines in the revenue generated from the real estate transfer, sales, and tobacco taxes. School Aid Fund revenue in FY 2006-07 came in stronger than was expected. Compared with the May 2007 consensus revenue estimate, SAF revenue was up $76.2 million. The preliminary year-end SAF revenue for FY 2006-07 also is presented in Table 4.

REVISED REVENUE ESTIMATES FOR FY 2007-08

General Fund/General Purpose and SAF revenue is expected to total $20.54 billion in FY 2007-08, which represents an increase of 5.5% from FY 2006-07. This anticipated strong rate of growth reflects recently enacted tax changes that go into effect during FY 2007-08. These tax changes are described below. While up 5.5% from FY 2006-07, the revised revenue estimates for FY 2007-08 are down $426.4 million from the revenue estimates on which the enacted FY 2007-08 budget was based, which reflected 1) the May 2007 consensus estimate of revenue before the tax changes and 2) the initial estimates of the enacted tax changes. This reduction in the estimate of the amount of GF/GP and SAF revenue that will be available in FY 2007-08 includes a reduction of $124.2 million that represents the amount by which a revision in the package of tax increases was short of being revenue neutral with the initial tax increase package, and a reduction of $302.1 million due to the revised slowdown in the forecast of economic activity. On a baseline basis, GF/GP and SAF revenue is expected to decline 1.2% in FY 2007-08 due to the expected slowdown in economic activity. The revised GF/GP and SAF revenue estimates for FY 2007-08 are summarized in Table 5.

Enacted Tax Changes

General Fund/General Purpose and School Aid Fund revenue will be boosted beginning in FY 2007-08 due to enactment of an increase in the personal income tax rate and the enactment of a new business tax. These tax changes, including the initial and modified tax increase packages, are summarized below.

Michigan Business Tax - Initial Enactment. In July 2007, Public Act (P.A.) 36 of 2007 enacted the new Michigan business tax to replace the single business tax. This tax will take effect January 1, 2008, when the repeal of the single business tax becomes effective. This new business tax creates a business income tax and a modified gross receipts tax. This new tax also provides a number of tax credits, many of which were available under the single business tax, and will be applied against the combined liabilities of the business income and gross receipts taxes. In addition, the Michigan business tax was the main part of a tax reform package that also included new personal property tax exemptions of varying amounts against the State education tax, the local 18-mill school tax, the industrial facilities tax, and the State utility property tax for personal property owned by industrial and commercial businesses. To hold the SAF harmless from the loss in property tax revenue and increased foundation payments to local school districts due to the loss in their local property tax revenue, a certain amount of the new Michigan business tax revenue is earmarked to the SAF. As shown in Table 6, as originally enacted, it was estimated the Michigan business tax would generate $1.4 billion in FY 2007-08, and $1.33 billion would go the General Fund and $136 million would go the SAF to hold it harmless from the negative financial consequences resulting from the new personal property tax exemptions.

Income Tax Increase. In early October, P.A. 94 of 2007 increased the income tax rate from 3.9% to 4.35%. This represents an 11.5% increase in the income tax. The 4.35% tax rate went into effect October 1, 2007, and will remain in effect until October 2011. Beginning in 2011, the rate will be lowered by 0.1 percentage point each year until it falls to 3.95% in October 2014, and then in October 2015 the rate will fall back to 3.9%. This law also created a new $250 exemption for disabled veterans. As shown in Table 6, it was originally estimated that this increase in the income tax rate would generate $744.8 million in FY 2007-08 and, based on the SFA's revised revenue estimates, it is still expected to generate $744.8 million. This was enacted as part of the overall budget agreement for FY 2007-08.

Use Tax on Selected Services. Also part of the original budget agreement for FY 2007-08 was an expansion of the use tax to include some selected services. This was enacted in P.A. 93 of 2007 and was to go into effect on December 1, 2007. It was estimated this new tax on services would generate $613.8 million in FY 2007-08. Of this amount, $409.2 million would go to the General Fund and $204.6 million would go to the SAF. On December 1, 2007, this expansion of the use tax was repealed.

Michigan Business Tax Increase. To replace the revenue lost by repealing the use tax on selected services, an increase in the Michigan business tax was enacted at the same time the use tax expansion was repealed. The major feature of this revision to the Michigan business tax was the creation of a surtax. Under this surtax, most business taxpayers will pay an extra amount equal to 21.99% of their Michigan business tax liability before the application of any credits. In addition, several other changes were made to the Michigan business tax. These changes include a reduction of the amount that can be claimed under the compensation credit, investment credit, and research and development credit; the creation of a new credit for a motorsports complex; the expansion of a special credit for a large retailer; an increase in the number of insurance companies that will qualify to claim the compensation credit; and some changes to the definitions of business income and gross receipts. In addition, the amount of the Michigan business tax revenue earmarked to the SAF was increased to replace the revenue the SAF would have received from the use tax. At the time these changes were enacted, it was estimated that they would generate $489.6 million in FY 2007-08, which is $124.2 million less than the $613.8 million that was foregone when the use tax on selected services was repealed.

Fiscal Impact of Tax Changes. As summarized in Table 6, these tax changes will generate an estimated $2.5 billion in GF/GP and SAF revenue in FY 2007-08. The initial tax change package was enacted after the May 2007 consensus revenue estimate and was part of the final budget agreement that was enacted in October and was expected to generate $2.76 billion in new revenue. The SFA's revised estimate of the modified tax change package is that it will generate $2.5 billion, which is down from the budget agreement by $254.2 million. Of this amount, $124.2 million of the reduction is due to the fact that the final tax package was not revenue neutral with the initial tax package. The remaining $130.0 million reduction in the revised estimate of the revenue the tax package will generate is due to the revised economic forecast.

Table 5

FY 2007-08 REVISED REVENUE ESTIMATES GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND (Millions of Dollars)			Change from FY 2006-07		
	FY 2006-07 Preliminary Final	FY 2007-08 Revised Estimate	Dollar Change	Percent Change	$ Change from Enact. Budget Revised Est.[1]
GENERAL FUND/GENERAL PURPOSE:					
Baseline Revenue[2]	$8,306.2	$8,089.5	$(216.7)	(2.6)%	$(154.1)
Tax Changes Not In Baseline	11.4	1,091.3	1,079.9	---	(139.5)
Revenue After Tax Changes					
Personal Income Tax					
Gross Collections	8,129.5	8,876.6	747.1	9.2	(22.0)
Less: Refunds	(1,687.3)	(1,826.1)	(138.8)	8.2	20.0
Net Income Tax Collections	6,442.2	7,050.5	608.3	9.4	(2.0)
Less: Earmarking to SAF	(2,110.3)	(2,091.3)	19.0	(0.9)	5.7
Campaign Fund	(1.5)	(1.5)	0.0	0.0	0.0
Net Income Tax to GF/GP	4,330.4	4,957.7	627.3	14.5	3.7
Other Taxes					
Single Business Tax[3]	1,816.1	631.2	(1,184.9)	(65.2)	(46.2)
Michigan Business Tax[3]	0.0	1,487.1	---	---	157.9
Sales	83.1	91.2	8.2	9.8	(5.8)
Use	920.0	927.0	7.0	0.8	(438.5)
Cigarette	225.4	221.8	(3.6)	(1.6)	(1.4)
Insurance Company Premiums	223.8	235.5	11.7	5.2	(6.3)
Telephone & Telegraph[3]	87.3	71.0	(16.3)	(18.7)	7.0
Estate	0.7	0.0	(0.7)	(100.0)	0.0
Oil & Gas Severance	72.0	65.5	(6.5)	(9.0)	6.0
Casino Wagering	46.1	16.0	(30.1)	(65.3)	(2.6)
All Other	139.7	127.1	(12.6)	(9.0)	(4.5)
Subtotal Other Taxes	3,614.2	3,873.5	259.3	7.2	(334.3)
Total Nontax Revenue	373.0	349.6	(23.4)	(6.3)	37.0
GF/GP REV. AFTER TAX CHANGES[3]	**$8,317.6**	**$9,180.8**	**$863.1**	**10.4%**	**$(293.7)**
SCHOOL AID FUND:					
Baseline Revenue[2]	$11,179.3	$11,155.9	$(23.5)	(0.2)%	$(111.2)
Tax Changes Not In Baseline	(26.0)	201.0	227.1	---	(21.4)
Revenue After Tax Changes					
Sales Tax	4,768.5	4,738.6	(30.0)	(0.6)	(109.7)
Lottery Revenue	748.9	750.0	1.1	0.1	43.0
State Education Property Tax[3]	2,081.0	2,073.9	(7.1)	(0.3)	(31.0)
Real Estate Transfer Tax	237.5	219.0	(18.5)	(7.8)	(12.0)
Michigan Business Tax[3]	0.0	341.0	---	---	205.0
Income Tax	2,110.3	2,091.3	(19.0)	(0.9)	(210.4)
Casino Tax	106.7	117.3	10.6	10.0	(1.0)
Other Revenue	1,100.3	1,026.0	(74.3)	(6.8)	(16.6)
SAF REV. AFTER TAX CHANGES	**$11,153.3**	**$11,357.1**	**$203.8**	**1.8%**	**$(132.7)**
BASELINE GF/GP AND SAF	**$19,485.6**	**$19,245.4**	**$(240.1)**	**(1.2)%**	**$(265.3)**
Tax & Revenue Changes	(14.6)	1,292.3	1,306.9	---	(161.0)
GF/GP & SAF REV. AFTER CHANGES[3]	**$19,471.0**	**$20,537.9**	**$1,066.9**	**5.5%**	**$(426.4)**
SALES TAX	$6,552.2	$6,511.3	$(40.9)	(0.6)%	$(150.0)

[1] Includes revenue estimates that were used in preparing the budget that was enacted in Oct. 2008, which includes the May 2007 revenue estimates and the estimates of the initial tax increase package. [2] FY 2006-07 is the base year for baseline revenue. [3] The single business tax will be repealed and the Michigan business tax will begin effective Jan. 1, 2008. These tax changes will have an impact on the General Fund and the SAF.

Table 6

TAX CHANGES ENACTED FOR FY 2007-08
GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND
ESTIMATED FISCAL IMPACT
(Millions of Dollars)

			Modified Enacted Tax Changes			
Tax Changes	Public Act	**Initial Enacted Tax Changes**[1)]	Original Estimate 12/10/07	Change from Initial Tax Changes	SFA Revised Estimates 12/21/07	Change from Initial Tax Changes
Michigan Business Tax & Related Tax Changes	PA 36 of '07 PA 145 of '07	$1,400.8	$1,890.4	$489.6	$1,760.4	$359.6
General Fund/General Purpose:						
Michigan Business Tax		1,329.2	1,616.3	287.1	1,487.1	157.9
Insurance Tax Increase		79.6	77.1	(2.5)	76.3	(3.3)
Utility Property Tax Personal Property Exemption		(8.0)	(8.0)	0.0	(8.0)	0.0
Subtotal GF/GP		1,400.8	1,685.4	284.6	1,555.4	154.6
School Aid Fund:						
Michigan Business Tax		136.0	341.0	205.0	341.0	205.0
State Education Tax Personal Property Exemption		(68.8)	(68.8)	0.0	(68.8)	0.0
Industrial Facilities Tax Personal Property Exemption		(67.2)	(67.2)	0.0	(67.2)	0.0
Subtotal SAF		0.0	205.0	205.0	205.0	205.0
Personal Income Tax Rate Increase from 3.9% to 4.35%	PA 94 of '07	$744.8	$744.8	$0.0	$744.8	$0.0
General Fund/General Purpose		744.8	744.8	0.0	744.8	0.0
School Aid Fund		0.0	0.0	0.0	0.0	0.0
Use Tax on Selected Services	PA 03 of '07	$613.8	$0.0	$(613.8)	$0.0	$(613.8)
General Fund/General Purpose		409.2	0.0	(409.2)	0.0	(409.2)
School Aid Fund		204.6	0.0	(204.6)	0.0	(204.6)
Total New Revenue		**$2,759.4**	**$2,635.2**	**(124.2)**	**$2,505.2**	**$(254.2)**
General Fund/General Purpose		2,554.8	2,430.2	(124.6)	2,300.2	(254.6)
School Aid Fund		204.6	205.0	0.4	205.0	0.4

1) Basis for FY 2007-08 Budget

General Fund/General Purpose

General Fund/General Purpose revenue will total an estimated $9.18 billion in FY 2007-08, which is up 10.4% or $863.1 million from FY 2006-07. This large increase reflects the additional revenue that will be realized due to the increase in the income tax rate and the new Michigan business tax. Based on the tax structure that was in place for FY 2007-08 when the May 2007 consensus revenue estimate was adopted, which included the repeal of the single business tax effective December 31, 2007, with no replacement, GF/GP revenue would have been down an estimated 17.3% or $1.44 billion from FY 2006-07 to an estimated $6.88 billion. The additional GF/GP revenue in FY 2007-08 from the tax increases totals an estimated $2.3 billion. Compared with the May consensus revenue estimate plus the initial estimate of the original tax change package, which was the basis for the enacted GF/GP budget for FY 2007-08, the revised revenue estimates are down $293.7 million. On a baseline basis, GF/GP revenue is expected to be down 2.6% in FY 2007-08 due to the downward revision in the level of economic activity in 2008.

School Aid Fund

School Aid Fund revenue from earmarked taxes and the lottery is expected to total $11.36 billion in FY 2007-08, which is up 1.8% from the FY 2006-07 level. The revenue derived from most of the major earmarked taxes is expected to decline in FY 2007-08 due to the weak level of economic activity forecast. The revenue from the sales, real estate transfer, and tobacco taxes is expected to be below the FY 2006-07 level. In addition, revenue collections from the State education and industrial facilities taxes also are expected to drop below their FY 2006-07 levels due to the weak economy and the impact of the new personal property tax exemptions that are part of the new Michigan business tax. Offsetting these declines will be the $341.0 million the SAF will receive from the Michigan business tax. This $341.0 million earmark from the Michigan business tax to the SAF includes $136.0 million for the loss in State education and industrial facilities tax revenue due to the new personal property tax exemptions and $205.0 million that would have been the SAF share of the repealed use tax on selected services. On a baseline basis, SAF revenue is expected to be down 0.2% in FY 2007-08. The SAF revenue estimate for FY 2007-08 is summarized in Table 5.

FY 2008-09 INITIAL REVENUE ESTIMATES

A modest improvement in economic activity, coupled with the full year impact of the increase in the income tax rate and the Michigan business tax, will help boost GF/GP and SAF revenue in FY 2008-09. Total GF/GP and SAF revenue will equal an estimated $21.0 billion in FY 2008-09, which is up 2.3% from the revised estimate for FY 2007-08. On a baseline basis, the modest improvement in the pace of economic activity will generate a revenue increase of 1.1%. The initial estimate of GF/GP and SAF revenue for FY 2008-09 is summarized in Table 7.

General Fund/General Purpose Revenue

While total GF/GP and SAF revenue is expected to be up in FY 2008-09 compared with the revised estimate for FY 2007-08, GF/GP revenue is not expected to post an increase. General Fund/General Purpose revenue will total an estimated $9.13 billion in FY 2008-09. This represents a decline of 0.6% or $55.5 million from the FY 2007-08 revised estimate. This decline will be due primarily to the new earned income tax credit and the fact that the GF/GP revenue generated from the new Michigan business tax will remain essentially flat with the combined revenue from the single business and Michigan business taxes in FY 2007-08, due largely to a planned increase in the amount of Michigan business tax revenue that will be earmarked to the SAF. Baseline GF/GP revenue is expected to be up 0.9% in FY 2008-09.

School Aid Fund

School Aid Fund revenue from all earmarked taxes and the lottery will total an estimated $11.88 billion in FY 2008-09, which represents an increase of 4.6% or $522.3 million from the revised estimate for FY 2007-08; however, this relatively large increase overstates the true increase in underlying SAF revenue expected in FY 2008-09. Beginning in FY 2008-09, the earmarked revenue from the Michigan business tax will include the amount needed to reimburse the SAF for increased foundation allowance payments it will have to make to local school districts that will experience a reduction in their local 18-mill school property tax as a result of the new personal property tax exemption that is part of the Michigan business tax package. In FY 2008-09, this additional earmarking will equal $341.6 million, bringing the total to $729.0 million. Adjusting for this large increase in the Michigan business tax earmark, which will be directly offset by an increase in SAF expenditures, SAF revenue will be up about 1.6% in FY 2008-09. This adjusted increase reflects modest improvement in most of the taxes that are earmarked to the SAF.

Major General Fund and School Aid Fund Taxes in FY 2008-09

Income Tax. Income tax revenue will total an estimated $7.0 billion in FY 2008-09, which represents a decrease of 0.6% or $41.6 million from the FY 2007-08 revised estimate. While gross collections (withholding, quarterly, and annual payments before refunds) will increase by an estimated 2.3%, income tax refunds will increase an estimated 13.4%, which will more than offset the gain in gross collections. The increase in refund payments will be primarily due to the new earned income tax credit. The earned income tax credit is scheduled to go into effect for the 2008 tax year and will be claimed by eligible taxpayers beginning in FY 2008-09 when they file their 2008 annual income tax return. It is estimated that taxpayers will qualify for $132.0 million in earned income tax credits that will be refunded to them in FY 2008-09. The increase in the tax rate from 3.9% to 4.35% will generate an estimated $815.3 million in FY 2008-09. Under the distribution formula, all of this additional revenue from the tax rate increase will go to the General Fund. The SAF will receive 23.3% of gross income tax collections, which equates to $2.11 billion in FY 2008-09, the same amount the SAF would have received if there were no increase in the tax rate. General Fund/General Purpose revenue will receive the remaining $4.89 billion in income tax revenue in FY 2008-09.

Sales Tax. Sales tax collections are expected to increase a modest 0.6% in FY 2008-09 to $6.55 billion. Of this total amount, $4.77 billion will be earmarked to the SAF and $97.4 million will go to the General Fund. Most of the remaining amount is earmarked constitutionally and statutorily for revenue sharing payments to local governments, but over the past several years, a significant portion of the amount earmarked statutorily has been diverted to the General Fund.

Use Tax. Use tax collections will total an estimated $1.4 billion in FY 2008-09. The GF/GP share, which equals two-thirds of use tax revenue, will total an estimated $932.6 million and the remaining one-third, equal to $466.3 million, will be earmarked to the SAF.

Tobacco Taxes. Tax collections from the cigarette and other tobacco products taxes will total an estimated $1.09 billion in FY 2008-09, which represents a decrease of 1.9% from the revised estimate for FY 2007-08. Of this amount, the SAF will receive $439.7 million and $213.3 million will go into GF/GP revenue.

Casino Tax. Through FY 2006-07, the State's tax on casinos was equal to 12.1% of gross receipts from gaming. The State's tax was increased from 8.1% to 12.1% in 2004. All of the revenue generated from the original 8.1% tax goes to the SAF, while the revenue from the 4.0 percentage point increase goes to the GF/GP budget (3.5%) and the Agriculture Equine Industry Development Fund (0.5%). A provision in the law that increased the tax rate by 4.0 percentage points requires that this increase be eliminated for each of the three Detroit casinos when their permanent facilities are fully operational. Two of the three Detroit casinos are now in their permanent facility and the third is expected to be in its permanent facility by the end of FY 2007-08. As a result, after totaling $159.4 million in FY 2006-07, casino tax revenue will total an estimated $135.5 million in FY 2007-08 and $122.0 million in FY 2008-09. Of this amount, the GF/GP share will drop from $46.1 million in FY 2006-07 to $16.0 million in FY 2007-08. If all three casinos are in their permanent facility by the end of FY 2007-08, as is expected, then the General Fund will not receive any casino revenue in FY 2008-09. Casino revenue earmarked to the SAF will increase to an estimated $117.3 million in FY 2007-08 from $106.7 million in FY 2006-07, and then increase to $122.0 million in FY 2008-09.

Table 7

FY 2008-09 INITIAL REVENUE ESTIMATES GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND (Millions of Dollars)				
			Change from FY 2007-08	
	FY 2007-08 Rev. Est.	FY 2008-09 Initial Est.	Dollar Change	Percent Change
GENERAL FUND/GENERAL PURPOSE:				
Baseline Revenue:	$8,089.5	$8,158.9	$69.3	0.9%
Tax Changes Not In Baseline:	1,091.3	966.4	(124.9)	---
Revenue After Tax Changes:				
Personal Income Tax				
Gross Collections	8,876.6	9,080.3	203.7	2.3
Less: Refunds	(1,826.1)	(2,071.4)	(245.3)	13.4
Net Income Tax Collections	7,050.5	7,008.9	(41.6)	(0.6)
Less: Earmarking to SAF	(2,091.3)	(2,112.5)	(21.2)	1.0
Campaign Fund	(1.5)	(1.5)	0.0	0.0
Net Income Tax to GF/GP	4,957.7	4,894.9	(62.8)	(1.3)
Other Taxes				
Single Business Tax[1)]	631.2	0.0	(631.2)	(100.0)
Michigan Business Tax[1)]	1,487.1	2,112.4	625.3	42.0
Sales	91.2	97.4	6.1	6.7
Use	927.0	932.6	5.6	0.6
Cigarette	221.8	213.3	(8.5)	(3.8)
Insurance Company Premiums[1)]	235.5	252.8	17.3	7.3
Telephone & Telegraph	71.0	79.0	8.0	11.3
Estate	0.0	0.0	0.0	---
Oil & Gas Severance	65.5	67.9	2.4	3.7
Casino Wagering	16.0	(0.0)	(16.0)	(100.1)
All Other	127.1	129.4	2.3	1.8
Subtotal Other Taxes	3,873.5	3,884.8	11.3	0.3
Total Nontax Revenue	349.6	345.6	(4.0)	(1.1)
GF/GP REVENUE AFTER TAX CHANGES	**$9,180.8**	**$9,125.3**	**$(55.5)**	**(0.6)%**
SCHOOL AID FUND:				
Baseline Revenue:	$11,155.9	$11,291.7	$135.8	1.2%
Tax Changes Not In Baseline:	201.0	587.7	386.7	---
Revenue After Tax Changes:				
Sales Tax	4,738.6	4,768.3	29.7	0.6
Lottery Revenue	750.0	755.0	5.0	0.7
State Education Property Tax	2,073.9	2,151.2	77.3	3.7
Real Estate Transfer Tax	219.0	216.0	(3.0)	(1.4)
Michigan Business Tax[1)]	341.0	729.0	388.0	113.8
Income Tax	2,091.3	2,112.6	21.3	1.0
Casino Tax	117.3	122.0	4.7	4.0
Other Revenue	1,026.0	1,025.3	(0.7)	(0.1)
SAF REVENUE AFTER TAX CHANGES	**$11,357.1**	**$11,879.4**	**$522.3**	**4.6%**
BASELINE GF/GP AND SAF	$19,245.4	$19,450.6	$205.2	1.1%
Tax & Revenue Changes	1,292.3	1,554.1	261.8	---
GF/GP & SAF REV. AFTER TAX CHANGES[1)]	**$20,537.9**	**$21,004.7**	**$466.8**	**2.3%**
SALES TAX	$6,511.3	$6,552.1	$40.8	0.6%

Note: FY 2006-07 is the base year for baseline revenue.

[1)] The single business tax will be repealed and the Michigan business tax will begin effective January 1, 2008. These tax changes will have an impact on both the General Fund and the School Aid Fund.

State Education Property Tax. The State education property tax is expected to generate $2.07 billion in FY 2007-08, representing a decrease of 0.3%. This decline in the State education tax revenue will be due in part to the slowdown in the housing market, but more significantly to the new personal property tax exemption that is part of the Michigan business tax. In FY 2008-09, State education property tax revenue will increase an estimated 3.7% to $2.15 billion.

Lottery. Net lottery revenue will total an estimated $755.0 million in FY 2008-09, which will be up an estimated 0.7% from the $750.0 million expected in FY 2007-08.

Michigan Business Tax. The new Michigan business tax will generate an estimated $2.84 billion in FY 2008-09, which will represent the first full fiscal year of this tax. Of this total amount, $2.11 billion will go the General Fund and $729.0 million will go to the SAF.

SENATE FISCAL AGENCY BASELINE REVENUE FORECAST HISTORY

The history of the Senate Fiscal Agency's and consensus estimates for GF/GP and SAF baseline revenue for FY 2006-07 and FY 2007-08 is presented in Tables 8 and 9. Baseline estimates are used to track the forecast history for these two fiscal years in order to avoid the wide swings in estimated revenue that occur when tax changes are enacted. In addition, in order to provide an accurate comparison, all of the previous baseline estimates made for FY 2006-07 and FY 2007-08 have been adjusted to reflect a common base year.

The initial estimate for FY 2006-07 GF/GP and SAF baseline revenue was made in January 2006 at $19.91 billion, as shown in Table 8. The revenue estimates were raised in May 2006 by $110.0 million. In January 2007, the estimate was lowered by a significant $538.8 million and then was lowered again in May 2007 by $207.2 million. The revised revenue level presented in this report, based on preliminary year-end revenue data from the Department of Treasury, increased the GF/GP and SAF baseline revenue $207.6 million or 1.1% from the May 2007 consensus estimate; however, compared with the initial estimate made in January 2006, the revised preliminary final estimate of GF/GP and SAF baseline revenue for FY 2006-07 is down $428.2 million or 2.2%.

The initial GF/GF and SAF baseline revenue estimate for FY 2007-08 was made in January 2007 at $19.86 billion, as shown in Table 9. This estimate was decreased $359.6 million at the May 2007 Consensus Revenue Estimating Conference. The Senate Fiscal Agency's revised estimates presented in this report, decreased GF/GP and SAF baseline revenue $254.4 million or 1.3% from the May 2007 consensus estimate. Compared with the initial estimate made in January 2007, the Senate Fiscal Agency's revised estimate of GF/GP and SAF baseline revenue for FY 2007-08 is down $614.0 million or 3.1%.

Table 8

CHANGES IN SENATE FISCAL AGENCY BASELINE REVENUE ESTIMATES FOR FY 2006-07 (Millions of Dollars)			
Forecast Date	**GF/GP**	**SAF**	**Total**
January 11, 2006	$8,332.5	$11,581.2	$19,913.7
January 12, 2006[a)]	8,392.3	11,606.0	19,998.3
May 15, 2006	8,444.6	11,562.6	20,007.2
May 17, 2006[a)]	8,455.8	11,568.1	20,023.9
January 16, 2007	8,172.9	11,287.7	19,460.6
January 18, 2007[a)]	8,236.7	11,248.4	19,485.1
May 17, 2007	8,230.0	11,113.4	19,343.4
May 18, 2007 [a)]	8,175.2	11,102.7	19,277.9
December 21, 2007	8,306.2	11,179.3	19,485.5
Change From Previous Estimate:			
Dollar Change	$131.0	$76.6	$207.6
Percent Change	1.6%	0.7%	1.1%
Change From Initial Estimate:			
Dollar Change	($26.3)	($401.9)	($428.2)
Percent Change	(0.3)%	(3.5)%	(2.2)%

Note: Baseline base year equals FY 2006-07.

a) Consensus estimate between the Senate Fiscal Agency, House Fiscal Agency, and Department of Treasury.

Table 9

CHANGES IN SENATE FISCAL AGENCY BASELINE REVENUE ESTIMATES FOR FY 2007-08 (Millions of Dollars)			
Forecast Date	**GF/GP**	**SAF**	**Total**
January 16, 2007	$8,293.5	$11,565.9	$19,859.4
January 18, 2007[a)]	8,345.0	11,534.8	19,879.8
May 17, 2007	8,232.8	11,288.9	19,521.7
May 18, 2007[a)]	8,210.5	11,289.3	19,499.8
December 21, 2007	8,089.5	11,155.9	19,245.4
Change From Previous Estimate:			
Dollar Change	($121.0)	($133.4)	($254.4)
Percent Change	(1.5)%	(1.2)%	(1.3)%
Change From Initial Estimate:			
Dollar Change	($204.0)	($410.0)	($614.0)
Percent Change	(2.5)%	(3.5)%	(3.1)%

Note: Baseline base year equals FY 2006-07.

a) Consensus estimate between the Senate Fiscal Agency, House Fiscal Agency, and Department of Treasury.

BUDGET STABILIZATION FUND

The Counter-Cyclical Budget and Economic Stabilization Fund (BSF) was established by Public Act (P.A.) 76 of 1977. The BSF is a cash reserve to which the State, in years of economic growth, adds revenue, and from which, in years of economic recession, the State withdraws revenue. The Fund's purposes are to mitigate the adverse effects on the State budget of downturns in the business cycle and to reserve funds that can be available during periods of high unemployment for State projects that will increase job opportunities.

The requirements for contributions to and withdrawals from the BSF are established in State law. By statute, revenue may be added to the BSF when Michigan personal income, less transfer payments and adjusted for inflation, increases by more than 2.0%. When the growth in real personal income less transfer payments is over 2.0%, the pay-in to the BSF is equal to the percentage growth in excess of 2.0% multiplied by the total General Fund/General Purpose (GF/GP) revenue.

Funds may be transferred out of the BSF for budget stabilization purposes when Michigan personal income less transfer payments, adjusted for inflation, decreases on a calendar-year basis. The withdrawal equals the percentage decline in adjusted real personal income multiplied by the annual GF/GP revenue. Thus, funds contributed to the BSF in growth years are used to supplement current revenue during a recession, reducing the need either to increase taxes or to reduce State services in a time of poor economic conditions.

Withdrawals from the BSF also are permitted for State job creation programs in times of high unemployment. When the State's unemployment rate averages between 8.0% and 11.9% during a calendar quarter, 2.5% of the balance in the BSF may be withdrawn during the subsequent quarter and appropriated for projects that will create job opportunities. If the unemployment rate averages 12.0% or higher for a calendar quarter, up to 5.0% of the BSF balance may be withdrawn.

In order for any payment into or out of the BSF actually to occur under either the personal income or the unemployment rate formula described above, the payment must be appropriated by the Legislature. In addition, the Legislature may appropriate transfers into or out of the BSF even if the formulas do not trigger a transfer. For example, in FY 1998-99, the Legislature appropriated a transfer into the BSF of $55.2 million in response to the personal income formula; however, the Legislature also appropriated to the BSF the ending balance of the General Fund/General Purpose budget, which equaled $189.2 million. Also in FY 1998-99, the Legislature appropriated the transfer of $73.7 million from the BSF to the School Aid Fund to finance scheduled payments to K-12 school districts required under the *Durant* court case.

Table 10 presents the recent history of the BSF in terms of actual transfers into and out of the Fund, interest earnings, and year-end balances from FY 1998-99 through FY 2006-07. Also presented in this table are the SFA's estimates for FY 2007-08 and FY 2008-09. The BSF year-end balance as a percentage of GF/GP and SAF revenue is shown in Figure 12, and the estimated economic stabilization trigger calculations for FY 2007-08 and FY 2008-09 are presented in Table 11.

FY 2006-07

In FY 2006-07, the BSF had a beginning balance of $2.0 million. During the fiscal year there were no payments into or out of the fund, but an estimated $0.1 million in interest was earned, leaving an ending balance of $2.1 million in FY 2006-07.

FY 2007-08 AND FY 2008-09

Based on the SFA's revised estimates for personal income, transfer payments, and the Detroit Consumer Price Index (CPI), the budget stabilization formula triggers payments out of the Fund equal to $180.1 million in FY 2007-08 and another $23.6 million in FY 2008-09, as shown in Table 11. Given that there is only $2.1 million in the BSF and given that no additional transfers into the BSF were appropriated as part of the FY 2007-08 enacted budget, no transfers out of the BSF are anticipated in either FY 2007-08 or FY 2008-09.

Table 10

BUDGET AND ECONOMIC STABILIZATION FUND
TRANSFERS, EARNINGS AND FUND BALANCE
FY 1998-99 TO FY 2007-08 ESTIMATE
(Millions of Dollars)

Fiscal Year	Pay-In	Interest Earned	Pay-Out	Fund Balance
1998-99	$244.4	$51.2	$73.7	$1,222.5
1999-00	100.0	73.9	132.0	1,264.4
2000-01	0.0	66.7	337.0	994.2
2001-02	0.0	20.8	869.8	145.2
2002-03	9.1	1.8	156.1	0.0
2003-04	81.3	0.0	0.0	81.3
2004-05	0.0	2.0	81.3	2.0
2005-06	0.0	0.0	0.0	2.0
Senate Fiscal Agency estimates:				
2006-07	0.0	0.1	0.0	2.1
2007-08	0.0	0.1	0.0	2.2
2008-09	0.0	0.1	0.0	2.3

Figure 12

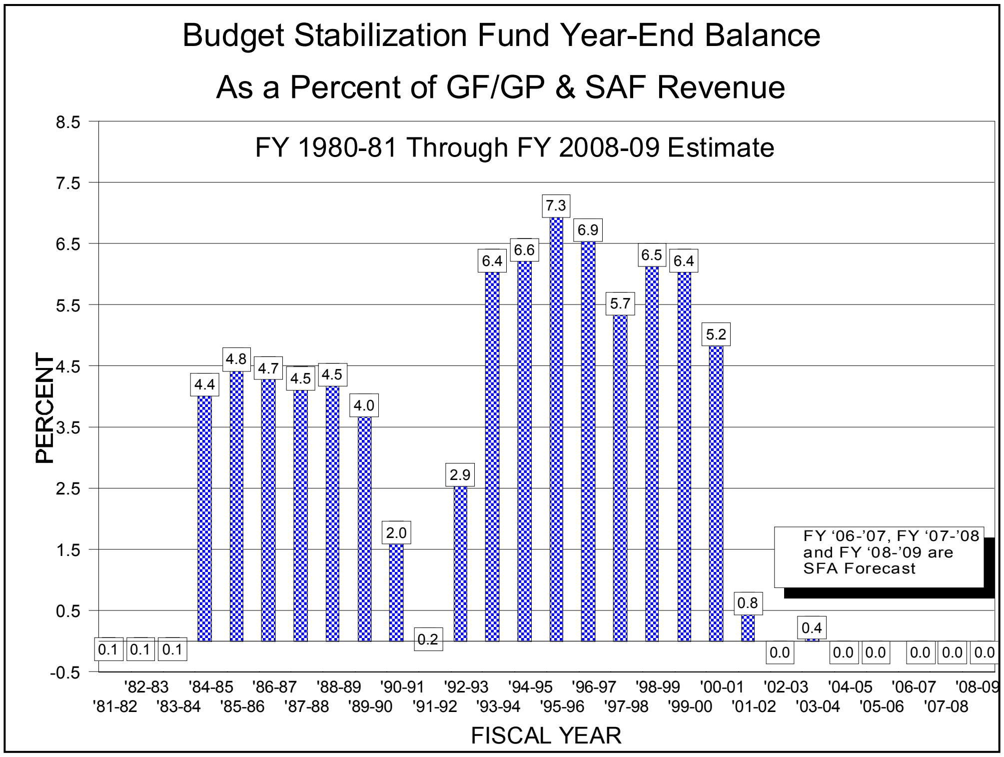


Table 11

ESTIMATED ECONOMIC AND BUDGET STABILIZATION FUND TRIGGER FY 2007-08 AND FY 2008-09 (Millions of Dollars)			
	CY 2007	**CY 2008**	**CY 2009**
Michigan Personal Income (MPI)	$353,657	$357,199	$367,962
Less: Transfer Payments	59,482	62,960	66,961
Subtotal	$294,175	$294,239	$301,001
Divided by: Detroit CPI, 12 months average ending June 30 (1982-84=1)	1.986	2.026	2.078
Equals: Real Adjusted MPI	$148,124	$145,219	$144,843
Percent Change from Prior Year		(0.96)%	(0.26)%
Excess Over 2.0%		0.00%	0.00%
		FY 2007-08	**FY 2008-09**
Multiplied by: Estimated GF/GP Revenue		$9,180.8	$9,125.3
Equals: Transfer to the BSF		$0.0	$0.0
OR Transfer from the BSF		$180.1	$23.6

Note: Numbers may not add due to rounding.
CY = Calendar Year; FY = Fiscal Year

COMPLIANCE WITH STATE REVENUE LIMIT

Article IX, Section 26 of the Michigan Constitution establishes a limit on the amount of revenue State government may collect in any fiscal year. This section of the Constitution was adopted by a vote of the people in 1978 and the limit was first applicable in FY 1979-80. In the first 15 years this revenue limit was in effect (FY 1979-80 to FY 1993-94), the revenue limit was never exceeded. The largest gap between revenue and the limit occurred in FY 2005-06, when State revenue was $4.9 billion below the revenue limit. In FY 1994-95, State revenue exceeded the revenue limit, for the first time, by $109.6 million. This was due to new State revenue being generated as part of the school financing reform that was enacted in 1994. In FY 1995-96 through FY 1997-98, revenue fell below the revenue limit again. In FY 1998-99 and FY 1999-2000, revenue exceeded the limit, but not by enough to require refunds to be paid to taxpayers. In FY 2000-01 through FY 2005-06, revenue fell well below the revenue limit. Based on the SFA's latest economic forecast and revenue estimates, it is estimated that revenue subject to the revenue limit remained well below the revenue limit in FY 2006-07 and, despite increases in the income and Michigan business taxes, it will remain well below the limit in FY 2007-08 and FY 2008-09.

THE REVENUE LIMIT

The revenue limit specifies that for any fiscal year, State government revenue may not exceed a certain percentage of Michigan personal income. The Constitution requires that the limit be calculated each year using the percentage that State government revenue in FY 1978-79 was of Michigan personal income in calendar year 1977. This calculation equals 9.49%. Therefore, for any fiscal year, State government revenue may not exceed 9.49% of Michigan total personal income for the calendar year prior to the calendar year in which the fiscal year begins. For instance, in FY 2006-07, State government revenue may not exceed 9.49% of personal income for calendar year 2005. Given that Michigan personal income for 2005 equaled $331,304 million, the revenue limit for FY 2006-07 is $31,441 million.

State government revenue subject to the limit includes total State government tax revenue and all other State government revenue, such as license fees, and interest earnings. For purposes of the limit, State government revenue does not include Federal aid. Personal income is a measure of the total income received by individuals, including wages and salaries, proprietors' income, interest and dividend income, rental income, and transfer payments. It is the broadest measure of overall economic activity for the State of Michigan and is estimated by the U.S. Department of Commerce's Bureau of Economic Analysis.

REQUIREMENTS IF REVENUE LIMIT IS EXCEEDED

If final revenue exceeds the revenue limit, the Constitution and State law provide procedures to deal with this event. If revenue exceeds the limit by less than 1%, the excess revenue must be deposited into the Budget Stabilization Fund. If the revenue limit is exceeded by 1% or more, the excess revenue must be refunded to income tax and business tax payers, on a pro rata basis. These refunds would be given to taxpayers who file an annual income tax or SBT (Michigan business tax beginning in 2008) return in the following fiscal year, because these taxpayers would have made withholding and quarterly estimated payments during the fiscal year when the revenue limit was exceeded. The law requires that these refunds occur in the fiscal year following the filing of the report which determines that the limit was exceeded. This report for any particular fiscal year is typically issued in the spring following the end of the fiscal year.

REVENUE LIMIT COMPLIANCE PROJECTIONS

Based on preliminary year-end data for FY 2006-07, and the SFA's revised revenue estimates for FY 2007-08 and the initial estimates for FY 2008-09, it is estimated that revenue subject to the constitutional revenue limit will remain well below the revenue limit for each of these fiscal years. The SFA's estimates of the State's compliance with the revenue limit for FY 2006-07 through FY 2008-09 are presented in Table 12.

FY 2006-07

Based on Michigan's personal income for calendar year 2005, the revenue limit in FY 2006-07 is equal to $31.4 billion. Revenue subject to the limit equaled an estimated $26.2 billion in FY 2006-07, based on preliminary final revenue. As a result, it is estimated that revenue fell short of the revenue limit by $5.2 billion, or 16.6%, in FY 2006-07.

FY 2007-08

In FY 2007-08, the revenue limit will equal 9.49% of Michigan's personal income in calendar year 2006. According to the U.S. Department of Commerce's Bureau of Economic Analysis, the estimate of Michigan personal income for 2006 is to $341.1 billion. The revenue limit is 9.49% of this personal income level, which equals $32.4 billion. Based on the SFA's revised revenue estimates for FY 2007-08, revenue subject to the limit will total $27.4 billion. As a result, it is estimated that revenue subject to the limit will fall below the revenue limit in FY 2007-08 by $5.0 billion or 15.5%. The amount by which revenue falls below the limit is expected to narrow slightly in FY 2007-08 due to the enacted increases in the income and Michigan business taxes.

FY 2008-09

In FY 2008-09, the revenue limit will equal 9.49% of Michigan's personal income in calendar year 2007. Based on the SFA's economic forecast, Michigan personal income in calendar 2007 will equal an estimated $353.7 billion, so the revenue limit is estimated at $33.6 billion for FY 2008-09. Based on the SFA's initial revenue estimates for FY 2008-09, revenue subject to the revenue limit will equal an estimated $28.0 billion. As a result, it is estimated that revenue subject to the limit will fall below the limit by $5.5 billion or 16.5% in FY 2008-09.

Table 12

COMPLIANCE WITH CONSTITUTIONAL REVENUE LIMIT
SECTION 26 OF ARTICLE IX OF THE STATE CONSTITUTION
FY 2005-06 THROUGH FY 2008-09 ESTIMATE
(Millions of Dollars)

	FY 2005-06 Final	FY 2006-07 Estimate	FY 2007-08 Estimate	FY 2008-09 Estimate
Revenue Subject to Limit				
Revenue:				
General Fund/General Purpose (baseline)	$8,185.2	$8,306.2	$8,089.5	$8,158.9
Revenue Sharing (baseline)	1,645.5	1,611.7	1,596.6	1,600.0
School Aid Fund (baseline)	11,085.4	11,179.3	11,155.9	11,291.7
Transportation Funds	2,182.4	2,205.4	2,198.0	2,208.0
Other Restricted Non-Federal Aid Revenue	2,666.0	2,900.0	3,000.0	3,200.0
Adjustments:				
GF/GP Federal Aid	(20.1)	18.8	20.0	20.0
GF/GP Balance Sheet Adjustments	80.9	11.4	1,091.3	966.4
SAF Balance Sheet Adjustments	(3.3)	(26.0)	201.0	587.7
Total Revenue Subject to Limit	**$25,822.0**	**$26,206.8**	**$27,352.3**	**$28,032.7**
Revenue Limit				
Personal Income:				
Calendar Year	**CY 2004**	**CY 2005**	**CY 2006**	**CY 2007**
Amount	$324,134	$331,304	$341,075	$353,657
Revenue Limit Ratio	9.49%	9.49%	9.49%	9.49%
Revenue Limit	$30,760.3	$31,440.7	$32,368.0	$33,562.0
1.0% of Limit	307.6	314.4	323.7	335.6
Amount Under (Over) Limit	**$4,938.3**	**$5,233.9**	**$5,015.7**	**$5,529.3**
Percent Below Limit	16.1%	16.6%	15.5%	16.5%

ESTIMATE OF YEAR-END BALANCES

This section of the Senate Fiscal Agency's (SFA's) report provides details of the estimated year-end balances of the General Fund/General Purpose (GF/GP) budget and School Aid Fund (SAF) budget for FY 2006-07 and FY 2007-08. This section of the report also contains a review of the issues that the Governor and Legislature will be facing in the development and enactment of the FY 2008-09 State budget.

Table 13 provides a summary of the estimated year-end balances for the FY 2006-07 and FY 2007-08 GF/GP and SAF budgets. The final accounting of revenue and expenditures for FY 2006-07 has not been completed, but the SFA is estimating that when the FY 2006-07 book-closing process is completed, the GF/GP budget will have a $242.3 million year-end balance and the SAF budget will close with a $76.2 million year-end balance. Pursuant to statutory authorization, the final level of the FY 2006-07 GF/GP and SAF year-end balances will carry forward into FY 2007-08. A comparison of the SFA estimates of FY 2007-08 GF/GP revenue and expenditures leads to a $75.5 million projected budget balance. A comparison of the current SFA estimates of FY 2007-08 SAF revenue and expenditures projects to a $58.5 million positive balance.

The initial look ahead at the FY 2008-09 GF/GP budget leads to the conclusion that modest revenue growth, combined with enacted tax changes, will almost certainly result in considerable restraint in appropriation growth. In regard to the FY 2008-09 SAF budget, sufficient revenue should be available to provide for a modest increase in per pupil State funding. The majority of this per pupil funding increase can be attributed to a continued decline in the number of pupils.

Table 13

GENERAL FUND/GENERAL PURPOSE AND SCHOOL AID FUND ESTIMATED YEAR-END BALANCES (Millions of Dollars)

	FY 2006-07 Estimate	FY 2007-08 Estimate
General Fund/General Purpose	$242.3	$75.5
School Aid Fund	76.2	58.5

FY 2006-07 YEAR-END BALANCE

The Office of the State Budget (OSB) is expected to complete the final accounting of FY 2006-07 State revenue and expenditures by December 31, 2007. Once the final accounting is completed, the State will publish the FY 2006-07 Comprehensive Annual Financial Report.

Based on the year-to-date accounting of FY 2006-07 GF/GP revenue and expenditures, the SFA is now estimating that the GF/GP budget will close the year with a $242.3 million balance. The SFA is estimating that the FY 2006-07 SAF budget will close the year with a $76.2 million balance.

Table 14 provides a summary of the current SFA estimate of a $242.3 million year-end balance in the FY 2006-07 GF/GP budget. Pursuant to statutory requirements, the actual level of the FY 2006-07 year-end balance will carry forward and be available as an FY 2007-08 GF/GP revenue source. The $242.3 million year-end balance represents a considerable improvement over the estimates used in May 2007 when the Legislature and Governor agreed on the final actions to eliminate a projected FY 2006-07 GF/GP budget deficit. The improvements in the FY 2006-07 GF/GP budget situation can be attributed to increased revenue and restrained spending.

Table 14

FY 2006-07 GENERAL FUND/GENERAL PURPOSE REVENUE, EXPENDITURES, AND YEAR-END BALANCE (Millions of Dollars)	December 2007 SFA Estimate
Revenue	
Beginning Balance	$ 2.5
Ongoing Revenue:	
Ongoing Revenue Estimate	8,317.7
Revenue Sharing Freeze	540.8
Shift of Short-Term Borrowing Costs to School Aid Fund	22.8
Subtotal Ongoing Revenue	8,881.3
One-Time Revenue Sources:	
Forensic Center Settlement Revenue	7.8
Liquor Purchase Revolving Fund Transfer to General Fund	4.0
Consumer Finance Fees Transfer to General Fund	7.3
Executive Order 2007-3 (Revenue Items)	35.7
Tobacco Securitization Borrowing (Public Act 18 of 2007)	207.2
Convention Facilities Fund Transfer	35.0
Comprehensive Transportation Fund Transfer	5.3
21st Century Jobs Fund Transfer	30.0
State Campaign Fund Transfer	7.2
Michigan Conservation Corps Fund Transfer	20.0
Subtotal One-Time Revenue Sources	359.5
Total Revenue	**$9,243.3**
Expenditures	
Initial Enacted Appropriations	$9,222.8
Supplemental Appropriations (Public Act 3 of 2007)	17.6
Supplemental Appropriations (Public Act 7 of 2007)	0.0
Supplemental Appropriations (Public Act 17 of 2007)	69.5
Supplemental Appropriations (Public Act 36 of 2007)	1.0
Supplemental Appropriations (Public Act 41 of 2007)	73.9
Supplemental Appropriations (Public Act 93 of 2007)	0.1
Supplemental Appropriations (Public Act 94 of 2007)	0.1
Supplemental Appropriations (Public Act 142 of 2007)	8.0
Subtotal Supplemental Appropriations	170.2
Executive Order 2007-3 (Appropriation Reductions)	(274.2)
Health Care Advance Account Transfer to Restricted Revenue Accounts	6.2
Restoration of Auto Theft Prevention Reduction in EO 2007-3	4.0
Projected Year-End Appropriation Lapses	(128.0)
Total Expenditures	**$9,001.0**
Projected Year-End Balance	**$ 242.3**

It now appears that actual FY 2006-07 GF/GP revenue collections will exceed the May 2007 consensus revenue estimate by $130.3 million. Final GF/GP expenditures appear to be $128.0 million below the appropriated levels resulting from lapsed appropriations in State departments. This combination of increased revenue and spending reductions, coupled with other minor adjustments, leads to the $242.3 million projected budget balance.

On the revenue side of the FY 2006-07 GF/GP budget ledger, the SFA is now estimating that revenue will total $9.2 billion. This represents an increase of $213.3 million or 2.4% from the final level of FY 2005-06 GF/GP revenue. The major components of the FY 2006-07 GF/GP revenue total include $8.9 billion of ongoing revenue and $359.5 million of one-time revenue. The ongoing revenue consists of estimated GF/GP revenue, revenue resulting from the freeze in revenue sharing payments to cities, villages, and townships and the elimination of county revenue sharing payments, and the shifting of a portion of cash flow borrowing costs to the School Aid Fund. The one-time revenue included $207.2 million from borrowing against future tobacco settlement revenue payments and numerous other transfers of State restricted fund balances to the General Fund.

On the expenditure side of the FY 2006-07 GF/GP budget ledger, the SFA is now estimating that expenditures will total $9.0 billion. This represents a decrease of $26.5 million or 0.3% from the final level of FY 2005-06 expenditures. The major components of the FY 2006-07 GF/GP expenditure total include $9.2 billion of initial appropriations enacted in July 2006, nine supplemental appropriation bills totaling $170.2 million, a $274.2 million appropriation reduction implemented by Executive Order 2007-3, two other minor expenditure adjustments, and $128.0 million of GF/GP appropriation lapses.

Approximately 78.0% of the net GF/GP appropriation lapses occurred in the Departments of Community Health and Human Services. These lapses resulted from slight reductions in expenditures below the appropriated levels over the last quarter of the fiscal year. The $128.0 million of net GF/GP appropriation lapses represents an increase over the $85.2 million of GF/GP appropriation lapses recorded at the close of FY 2005-06. The FY 2006-07 GF/GP appropriation lapse is the largest year-end lapse since the FY 1997-98 budget closed the year with $138.6 million of GF/GP lapses.

Table 15 provides a summary of the current SFA estimate of a $76.2 million FY 2006-07 year-end balance in the SAF budget. Pursuant to statutory requirements, the actual level of the FY 2006-07 SAF year-end balance will carry forward and be available as an FY 2007-08 SAF revenue source. The $76.2 million year-end balance represents a considerable improvement over the estimates used in May 2007 when the Legislature and Governor agreed on final actions to eliminate a projected SAF budget deficit. The improvements in the budget can be attributed to increased SAF revenue.

On the revenue side of the FY 2006-07 SAF budget ledger, the SFA is now estimating that revenue will total $13.1 billion. This represents an increase of $402.0 million or 3.2% from the final level of FY 2005-06 SAF revenue. The major components of the revenue include $12.6 billion of ongoing revenue, which includes the appropriation of $1.4 billion of Federal funds and a $35.0 million grant from the GF/GP budget. One-time revenue totaled $469.8 million. Included in the one-time revenue sources were $207.8 million from borrowing against future tobacco settlement payments and savings of $262.0 million from changes in the assumptions used to make contributions to the Public School Employees Retirement System (PSERS).

On the expenditure side of the FY 2006-07 SAF budget ledger, the SFA is now estimating that expenditures will total $13.0 billion. This represents an increase of $325.8 million or 2.6% from the final level of FY 2005-06 expenditures. The final level of expenditures includes the initial appropriations for the fiscal year and numerous cost adjustments throughout the year, as well as a $5.0 million appropriation reduction contained in Public Act 6 of 2007.

Table 15

FY 2006-07 SCHOOL AID FUND REVENUE, EXPENDITURES, AND YEAR-END BALANCE (Millions of Dollars)	December 2007 SFA Estimate
Revenue	
Beginning Balance	$ 0.0
Ongoing Revenue:	
Ongoing Revenue Estimate	11,153.4
GF/GP Grant	35.0
Federal Aid	1,411.2
Subtotal Ongoing Revenue	12,599.6
One-Time Revenue:	
PSERS Retirement Contribution Rate (Mark to Market)	175.6
PSERS Interest Only on Unfunded Accrued Liability	86.4
Tobacco Securitization Borrowing (PA 18 of 2007)	207.8
Subtotal One-Time Revenue	469.8
Total Revenue	**$13,069.4**
Expenditures	
Initial Enacted Appropriations	$13,093.8
Midland Property Tax Case (PA 6 of 2007)	24.8
Refinance of Debt Service Payments (PA 6 of 2007)	(40.4)
Reduction of Various Categorical Grants (PA 6 of 2007)	(5.0)
Cost Adjustments (PA 6 of 2007)	(65.0)
Appropriation Lapses	(15.0)
Total Expenditures	**$12,993.2**
Projected Year-End Balance	**$ 76.2**

FY 2007-08 YEAR-END BALANCE

On October 1, 2007, the Michigan Legislature approved and the Governor signed into law increases in the rate of the State income tax and the expansion of the use tax to a list of certain services. At the same time, the Legislature approved and the Governor signed into law a 30-day extension of appropriations in place during FY 2006-07 for the month of October 2007. On October 31, 2007, the Legislature approved and the Governor signed into law the annual appropriation bills for FY 2007-08. On December 1, 2007, the Legislature approved and the Governor signed into law the repeal of the use tax on certain services and replaced most of this estimated revenue with an expansion of the Michigan business tax.

Based on the FY 2007-08 appropriations approved by the Legislature, the enacted tax policy changes, and the May 2007 consensus revenue estimate, the SFA was estimating that the FY 2007-08 GF/GP budget was in surplus by $102.1 million. Updating this estimate for the revised SFA revenue estimate and several assumptions concerning supplemental appropriations, leads the SFA to be currently estimating that the FY 2007-08 GF/GP budget is in surplus by $75.5 million. Table 16 provides a summary of this estimate.

Table 16

FY 2007-08 GENERAL FUND/GENERAL PURPOSE REVENUE, EXPENDITURES, AND YEAR-END BALANCE (Millions of Dollars)	December 2007 SFA Estimate
Revenue	
Beginning Balance	$ 242.3
Ongoing Revenue:	
Ongoing Revenue Estimate	9,180.7
Revenue Sharing Freeze	539.3
Revenue Sharing Hold Harmless Guarantee	(13.6)
Shift of Short-Term Borrowing Costs to School Aid Fund	22.8
Subtotal Ongoing Revenue	9,729.2
One-Time Revenue:	
Juror Compensation Fund Transfer to General Fund	2.3
Comprehensive Transportation Fund Transfer to General Fund	5.0
Transportation Economic Development Fund Transfer to General Fund	13.0
Financial Institutions Fund Shift to General Fund	2.0
Subtotal One-Time Revenue	22.3
Total Revenue	**$9,993.8**
Expenditures	
Initial Enacted Appropriations	$9,856.3
Projected Supplemental Appropriations:	
Presidential Primary Costs	10.0
Environmental Quality GF/GP Supplemental	11.0
Natural Resources GF/GP Supplemental	5.0
Medicaid School Health Disallowance	36.0
Subtotal Pending Supplemental Appropriations	62.0
Total Expenditures	**$9,918.3**
Projected Year-End Balance	**$ 75.5**

On the revenue side of the FY 2007-08 GF/GP budget ledger, the SFA is now estimating that revenue will total $10.0 billion. This estimate includes the $242.3 million GF/GP year-end balance carried forward from FY 2006-07, $9.7 billion of ongoing revenue, and $22.3 million of revenue from one-time sources. The total level of GF/GP revenue represents a $750.5 million or 8.1% increase from FY 2006-07 GF/GP revenue collections. The ongoing revenue includes $9.2 billion from the current law tax structure, $539.3 million from the freeze in revenue sharing payments, a $13.6 million revenue reduction from the hold harmless guarantee in regard to the revenue sharing freeze, and $22.8 million from the charging of a portion of the cash flow borrowing costs to the School Aid Fund. The one-time revenue sources are highlighted by the transfer of several State restricted fund revenue sources to the GF/GP budget.

On the expenditure side of the FY 2007-08 GF/GP budget ledger, the SFA is now estimating that expenditures will total $9.9 billion. This includes the initial level of enacted appropriations and the assumption that the Legislature will approve four GF/GP supplemental appropriation items. The supplemental appropriation items include: $10.0 million to reimburse local units of government for the costs of holding the January 15, 2008, presidential primary; $11.0 million to deal with funding shortfalls in the Department of Environmental Quality; $5.0 million to address funding shortfalls in the Department of Natural Resources; and $36.0 million to settle a dispute with the Federal government regarding Medicaid funding for school-based health clinics. The estimated level of FY

2007-08 GF/GP expenditures represents a $909.9 million or 10.1% increase from FY 2006-07 expenditures.

Absent any supplemental appropriations approved by the Legislature and signed into law by the Governor, the projected FY 2007-08 GF/GP year-end balance of $75.5 million will carry forward into FY 2008-09. This GF/GP balance also could be used as a cushion against any potential revenue revisions that might occur during the fiscal year.

The FY 2007-08 SAF budget originally enacted by the Legislature and approved by the Governor assumed a $12.5 million year-end balance. This estimate was based on the May 2007 consensus revenue estimate and enacted tax changes. The current SFA estimate of the FY 2007-08 SAF year-end balance is $58.5 million. This estimate is summarized in Table 17.

Table 17

FY 2007-08
SCHOOL AID FUND
REVENUE, EXPENDITURES, AND YEAR-END BALANCE
(Millions of Dollars)

	December 2007 SFA Estimate
Revenue	
Beginning Balance	$ 76.2
Ongoing Revenue Estimate	11,357.1
GF/GP Grant to School Aid Fund	34.9
Federal Revenue	1,479.3
Total Revenue	**$12,947.5**
Expenditures	
Initial Enacted Appropriations	$13,006.0
Revised Funding Cost Estimates	(117.0)
Total Expenditures	**$12,889.0**
Projected Year-End Balance	**$ 58.5**

On the revenue side of the FY 2007-08 SAF budget ledger, the SFA is now estimating that revenue will total $12.9 billion. This represents a $121.9 million or 0.9% decline from FY 2006-07 revenue collections. The SAF revenue total includes $76.2 million of surplus revenue carried forward from FY 2006-07, $11.4 billion of estimated State restricted revenue, a $34.9 million GF/GP grant to the SAF budget, and $1.5 billion of Federal aid.

On the expenditure side of the FY 2007-08 SAF budget ledger, the SFA is now estimating that expenditures will total $12.9 billion. This represents a $104.2 million or 0.8% decline from FY 2006-07 expenditures. The SAF expenditure total includes the initial level of enacted appropriations and a projected $117.0 million formula cost saving due to updated estimates. This $117.0 million formula cost saving includes $78.0 million from revised pupil counts, $25.0 million from increases in local property tax valuations, and $14.0 million from reduced costs of special education.

Absent any supplemental appropriations approved by the Legislature and signed into law by the Governor, the projected FY 2007-08 SAF year-end balance of $58.5 million will carry forward into FY 2008-09. This SAF balance also could be used as a cushion against any potential revenue revisions that might occur during the fiscal year.

FY 2008-09 STATE BUDGET OUTLOOK

Governor Granholm is required to submit her recommendation for the FY 2008-09 State budget to the Legislature no later than February 8, 2008. This budget recommendation will be balanced between estimated revenue and appropriations. Due to the restrained growth in FY 2008-09 GF/GP revenue that the SFA is estimating, along with several spending issues, the Governor will be forced to recommend a restrained level of appropriation growth in the FY 2008-09 GF/GP budget.

Table 18 provides an overview of the outlook for the FY 2008-09 GF/GP budget. The SFA is estimating that total FY 2008-09 GF/GP revenue equals $9.8 billion. This estimate reflects the carryforward of the FY 2007-08 year-end balance, the revenue generated from the current enacted revenue system, and an assumption involving a continuation of a freeze in revenue sharing payments made to local units of government. The revenue assumption also includes a continuation of the past practice of shifting a portion of the cash flow borrowing costs to the School Aid Fund.

Table 18

FY 2008-09
GENERAL FUND/GENERAL PURPOSE
BUDGET OUTLOOK
(Millions of Dollars)

	December 2007 SFA Estimate
Projected Revenue	
Beginning Balance	$ 75.5
Estimated Ongoing Revenue	9,125.3
Revenue Sharing Freeze	529.1
Shift of Short-Term Borrowing Costs to School Aid Fund	22.8
Total Estimated Revenue	**$9,752.7**
Potential Appropriations	
Freeze in FY 2008-09 Appropriations at FY 2007-08 Initial Levels	9,856.3
Potential Funding Imbalance	**$ (103.6)**
Other Potential Funding Issues:	
Elimination of Higher Education Funding Delay	$ (138.7)
Elimination of Community College Funding Delay	(25.8)
Increase in Federal Medicaid Match Rate	(208.0)
Medicaid Caseload, Utilization, and Cost Increases	170.0
Debt Service Increases	50.0
Revenue Sharing Payments to Counties	3.1
State Employee Economic Adjustments	80.0
Net Potential Funding Issues	**$ (69.4)**
Adjusted FY 2008-09 Potential Appropriations	**$9,786.9**
Potential Funding Imbalance	**$(34.2)**

If these FY 2008-09 GF/GP revenue assumptions are compared with the initial enacted level of FY 2007-08 GF/GP appropriations, a $103.6 million imbalance exists. There are several adjustments that will have to be made to the FY 2007-08 appropriation base during FY 2008-09. These include appropriation reductions of $138.7 million and $25.8 million to the higher education and community college budgets, respectively, to reflect the elimination of extra payments made to universities and community colleges during FY 2007-08 as a result of a funding delay enacted in FY 2006-07. The SFA is estimating that an increase in Michigan's Federal Medicaid match rate will result in a $208.0

million increase in Federal Medicaid funds and a corresponding decrease in GF/GP support for the Medicaid program compared with the prior fiscal year. The SFA is estimating that increases in Medicaid caseloads and utilization, and various cost increases will have the impact of increasing FY 2008-09 GF/GP Medicaid appropriations by $170.0 million. Debt service payments on bonds issued by the State Building Authority and general obligation bonds should increase during FY 2008-09 by $50.0 million. The State will be required to appropriate $3.1 million to counties for revenue sharing payments. These are payments to counties that have exhausted their reserves from the one-time change in county property tax collections. Finally, the cost of State employee health benefits and contribution rates to the various State retirement systems should increase GF/GP appropriations by $80.0 million. These adjustments will have the combined impact of reducing FY 2008-09 GF/GP appropriations by $69.4 million.

Therefore, a comparison of the FY 2008-09 GF/GP revenue and appropriation assumptions leads to a $34.2 million imbalance. This analysis assumes that all other GF/GP appropriations are funded in FY 2008-09 at the FY 2007-08 funding levels. Absent any changes in tax policy, the Governor and the Legislature can anticipate a FY 2008-09 GF/GP budget debate that will likely focus on proposals to reduce appropriations in order to ensure a balance between estimated revenue and appropriations.

Table 19 provides an overview of the outlook for the FY 2008-09 SAF budget. The SFA is estimating that total FY 2008-09 SAF revenue equals $13.5 billion. This estimate includes $58.5 million of surplus FY 2007-08 SAF revenue carried forward into FY 2008-09, $11.9 billion of State restricted SAF revenue, the continuation of the GF/GP grant to the SAF budget at the prior fiscal year level, and $1.5 billion of Federal aid.

Table 19

FY 2008-09
SCHOOL AID FUND
BUDGET OUTLOOK
(Millions of Dollars)

	December 2007 SFA Estimate
Projected Revenue	
Beginning Balance	$ 58.5
Estimated Ongoing Revenue	11,879.4
GF/GP Grant at FY 2007-08 Level	34.9
Federal Aid	1,479.3
Total Estimated Revenue	**$13,452.1**
Potential Appropriations	
Freeze in FY 2008-09 Appropriations at FY 2007-08 Initial Levels	$13,006.0
Potential Funding Issues:	
Adjustment for Reduction in Local Property Taxes	341.6
Pupil Count Reduction	(200.0)
Adjusted FY 2008-09 Potential Appropriations	**$13,147.6**
Potential Funding Balance	**$ 304.5**

On the appropriation side of the FY 2008-09 SAF budget outlook, if FY 2008-09 appropriations are frozen at the FY 2007-08 levels, they will equal $13.0 billion. The FY 2008-09 SAF appropriations will have to reflect a $341.6 million increase resulting from a reduction in local school district property taxes. This reduction was part of the implementation of the Michigan business tax and is offset by increased earmarking of Michigan business tax revenue to the SAF budget. The SFA is estimating that the total number of pupils funded in FY 2008-09 will decline by approximately 25,000 from the level funded in FY 2007-08. This decline in pupils funded results in approximately $200.0 million of savings for the State. The SFA is now projecting that the total number of pupils funded will have declined from a peak of 1,714,867 pupils in FY 2002-03 to a level of 1,629,000 in FY 2008-09. If the number of pupils funded during FY 2008-09 equaled the number funded in FY 2002-03, the FY 2008-09 SAF appropriations would have to be increased by approximately $687.0 million.

Therefore, a comparison of the FY 2008-09 estimate of SAF revenue and appropriations frozen at the prior-year initial enacted level leads to a $304.5 million potential funding balance. This potential funding balance equates to approximately $187 per pupil or a 2.6% increase in the minimum per pupil foundation allowance.