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CLIENT ALERT: Proposed State Budget 2016

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It is always interesting to see if the rhetoric in Lansing matches the facts when it comes to budgeting, in general, and the treatment of local governments, specifically. This year is certainly no exception.

For this year's review, I have taken a deeper look at the Governor's proposed budget, as presented on the State of Michigan's website. The specific link to the budget document is www.michigan.gov/documents/budget/Budget_all_together_2016_final_481096_7.pdf

In looking at the budget, I decided to review the period starting with Governor Snyder's first term in office, with the understanding that during his first year in office he was working with a budget that he inherited. Therefore, the review period includes Fiscal Years 2012 through the proposed 2016 budget to reflect those budget years in which Governor Snyder made the recommendations. This is an important period because it can be viewed against the backdrop of the difficult choices that needed to be made to restore the State's budget to fiscal security.

In addition, the review should also include the decisions that the State made regarding statutory (as opposed to Constitutional) revenue sharing for Cities, Villages, Townships and Counties in light of last year's accusations by the Michigan Municipal League that the State of Michigan underfunded local communities by at least six hundred and fifty million dollars.[1]

On the State of Michigan side of the equation, I have chosen to focus on the budgets of those departments headed by elected officials. Those budgets include the Attorney General, the Governor's Office, the Legislature (including the Legislative Auditor General), the Secretary of State and the Judiciary. Looking at the period of FY 2012 through the proposed FY 2016 budget, it is important to note that net total revenues[2] during the period increased by 12.53% from all sources while general fund, general purpose revenues increased by less than 8.8%.[3]

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[1] See "The Revenue Sharing Heist" by Anthony Minghine in the March/April 2014 Review Magazine, Michigan Municipal League:

"Hopefully you'll stick with me, as I'm about to drop the "b" word. From 2003-2013, sales tax revenues went from $6.6 *billion* to $7.72 *billion*. Over that same period, statutory revenue sharing declined from over $900 million annually to around $250 million. The state is now in an enviable position—revenues that exceeded expectations. It is posting large surpluses but has failed to take steps to restore local funding." http://www.mml.org/advocacy/great-revenue-sharing-heist.html

[2] All revenues after interfund transfers. See p.C-17 of the Budget report. www.michigan.gov/documents/budget/Budget_all_together_2016_final_481096_7.pdf

[3] The figure drops even further to 4.6% if one takes into account the general fund – general purpose budget adjustments proposed in the current budget.

Surprisingly, during this time of belt tightening and difficult financial choices, every single State of Michigan Office or Department headed by elected officials had a percentage budget increase in discretionary State General Fund-General Purpose funding that exceeded the GFGP revenue growth, and all offices except for the Judiciary exceeded that growth rate by a factor of at least 245%. Let's review:

- The Attorney General's Office increased from $29.6 million in FY12 to $36.8 million for FY16, an increase of 24.4%
- The Governor's Office increased from $4.45 million in FY12 to $5.92 million in FY16, an increase of 32.9%
- The Judiciary increased from $155.6 million in FY12 to $182.7 million in FY16, an increase of 17.4%
- The Legislative Auditor General increased from $11.6 million in FY12 to $15.5 million for FY16, an increase of over 33.3%
- The Legislature increased from $108.5 million in FY12 to $131.9 million in FY16, an overall increase of 21.6%
- The Secretary of State's Office increased from $11.3 million in FY12 to $17.2 million in FY16, an increase of over 52.4%

Again, to put these numbers in perspective, during the same time period, general fund – general purpose revenues only increased by 8.8% (or 4.6% if one takes GFGP budget adjustments into account).

According to a House Fiscal Agency report, dated January 2015, revenue sharing for Cities, Villages and Townships is not fairing quite as well. As one would expect, per-capita constitutionally guaranteed payments[4] to Cities, Villages, and Townships have grown consistent with sales tax revenue growth. However, discretionary statutory revenue sharing payments[5] remain $435 million below the FY 2001 peak. Similarly, on the County revenue sharing side of the equation, funding in FY 2015 still has not returned to the FY 2002 level.

To make matters worse, the State of Michigan has conditioned funding to local governments on their ability to achieve the accountability and transparency guidelines established by the State of Michigan. This means that the same State Government that has grown the budgets of its own elected officials on average by more than 250% of the growth rate of general fund revenue, is continuing to condition payments to local communities based on its own patriarchal views of those standards.

Reminds me of the old golden rule: those with the gold, make the rules.

But the more important issue is finding a way to incentivize the State to realize that the fiscal health of local communities is important to its own strength. It is simply illogical to assume that the State of Michigan could be viewed as financially strong while local communities and school districts enter financial distress at increasing rates.

[4] Constitutional revenue sharing is set at 15% of the 4% collection of gross sales tax.

[5] Statutory revenue sharing is set at 21.3% of the 4% collection of gross sales tax. Of this pool, Counties receive only 25.06% with the remaining 74.94% going to cities, villages and townships.

The solution is actually quite simple. So simple, in fact, that it is surprising that the solution has not occurred on its own. Bond rating agencies such as Fitch, S&P, and Moody's should take the fiscal health of local communities into account in evaluating the fiscal health of the State of Michigan. Cities, Villages, Townships, Counties and School Districts are, after all, creatures of the State. They could not exist and would not have any powers absent State authorization. Absent language in the State Constitution and state statute, the State would exercise all of the powers of these local units of government.

By shifting the oversight burden back to the State, the credit rating agencies can ensure that the people who hold the purse strings are responsible for all budget decisions that are made. This would finally align budgetary priorities with service delivery to all Michigan residents. It would remove the incentive to grow elected officials' budgets by more than double the growth rate of general fund revenues, while cutting revenue sharing to local communities in the name of accountability. More importantly, it would help put a much more pointed focus on the need for truly incentivizing regional collaboration efforts in an effort to drive efficiency in governmental operations.

It is time for real accountability in the delivery of governmental services. Holding the State of Michigan responsible for its own fiscal health as well as the fiscal health of all of the local units of government that it has created is an idea whose time is long past due.