

# Analyzing the Governor's FY2022 Budget Recommendation

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Citizens Research Council of Michigan

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## Robert Schneider, Senior Research Associate



- Work Experience
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## Craig Thiel, Research Director



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  - 2006 - present: Citizens Research Council
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## Revisiting 2020: Impact of COVID-19 on the State Budget



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## Onset of COVID-19: January/February 2020

- January 24: MIRS News – 2 persons in Washtenaw County and 1 in Macomb County being tested for Novel Coronavirus
- February 6: FY2021 Executive Budget proposal is released; no funding specific to COVID-19. Recommendation draws down almost all of the combined \$788 million balance in General Fund and School Aid Fund
- February 27: MIRS News – Chief Medical Officer Dr. Joneigh Khaldun addresses Senate Health Policy and Human Services Committee on Coronavirus; data shows 78,000 confirmed cases and 2,600 deaths globally

## Onset of COVID-19: March 2020

- March 3: MIRS News - Governor announces creation of four Coronavirus task forces; no confirmed cases in Michigan, but confirmed cases in 10 other states with two deaths
- March 10: MIRS News – Governor confirms first two “presumed positive” Coronavirus cases in Michigan and declares state of emergency; 63 Michiganders tested; 124 under active monitoring
- Executive Orders and Developments
  - March 12 – K-12 schools closed for 3 weeks; universities move to online learning
  - March 13 – Restrictions on events with 250 or more people
  - March 16 – Closure of restaurants, bars, coffee shops,

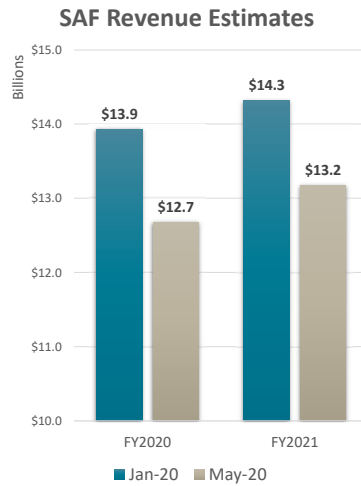
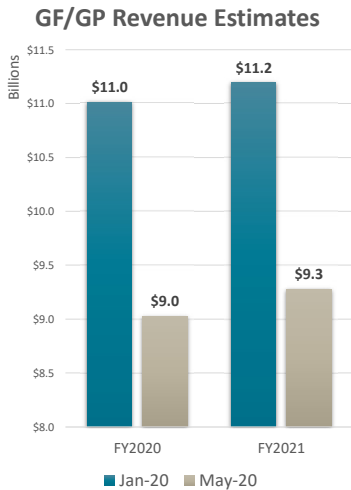
## Initial State Funding for COVID-19 Response

- Governor signs two supplemental appropriation bills on March 30 providing immediate funding for Coronavirus response
  - Administration and Legislature agree to vetoes of \$157 million in state funding that was part of an early March FY2020 budget deal
  - Funding is redirected to COVID-19 response efforts
    - \$50M GF/GP for health care system capacity
    - \$50M GF/GP for public health response efforts
    - \$50M reserved within Coronavirus Response Fund
  - Temporary “receive and expend” authority in budget language appropriated any new federal funding received for COVID-19 response efforts

## Major Federal Support for COVID-19 Response

- Coronavirus Relief Fund (CRF): distribution in late March provided \$3.1B to State of Michigan and \$792M to Detroit and largest counties: Wayne, Oakland, Macomb, and Kent
- FEMA support became available following federal declaration of emergency in Michigan on March 27; requires 25% state match but eventual FEMA guidance allows CRF funds to be used to meet that match requirement
- Enhanced Medicaid match: federal share of state Medicaid spending goes up 6.2% retroactive to January 1, 2020
- Centers for Disease Control Testing Funds: \$316.5M provided in May to cover testing, contact tracing and laboratory capacity

## Revenue Estimates Plummet in May



May 2020: Combined GF/GP and School Aid Fund (SAF) revenue projections down \$5.5B

FY2020 revenue forecast down \$3.2M, necessitating budget reductions mid-way through FY2020

Source: May 2020 CREC Final Summary.



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## Rewriting the FY2020 Budget

*July Budget Adjustments Save Over \$2.4 billion across GF/GP and SAF*

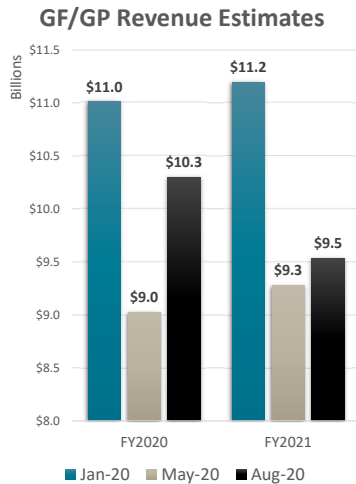
Budget/Revenue Savings	GF/GP (millions)	SAF (millions)
Federal CRF offsets state costs (Public Safety staff, K-12, Higher Education, Revenue Sharing, COVID Response)	\$696.5	\$456.0
Enhanced Federal Medicaid Match: applied Jan-Sep 2020	\$523.3	
Budget Stabilization Fund Deposit into School Aid Fund		\$350.0
GF/GP Shifted to School Aid Fund Budget	(\$211.0)	\$211.0
Work Project Cancellations and One-Time Fund Shifts	\$97.3	\$44.1
State Hiring Freeze and Temporary Layoff Savings	\$48.4	
Other Statewide Budget Savings	\$138.9	\$120.0
<b>Savings for Fund Balances</b>	<b>\$1,293.4</b>	<b>\$1,181.1</b>



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## Revenue Picture Greatly Improves in August



After finalizing the FY2020 budget, revenues revised up by \$2.3B across both major funds.

FY2021 estimates up a combined \$500M.

Source: August 2020 CREC Final Summary.



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## Finalizing the FY2021 Budget

*Improving Revenue Picture Largely Eliminates Remaining Shortfall*

- School Aid Fund surplus: \$355 million
  - Increase for K-12 schools and Community Colleges: \$187M
  - Remaining SAF balance is used to reduce GF/GP support by \$169M
- General Fund shortfall: \$502 million
  - Enhanced Medicaid match extended to first quarter FY2021: \$240M
  - GF/GP shifted from School Aid budget: \$169M
  - GF/GP budget reductions (\$255 million) exceed new GF/GP investments (\$241 million) to close remaining budget hole
- December supplemental – COVID-19 Response
  - \$92M GF/GP for COVID-19 vaccine and testing administration
  - \$30M (\$16.1M GF/GP) for hospital and nursing homes treating COVID-19 patients
  - \$106M GF/GP for grants to small businesses, entertainment venues and employees affected by the pandemic as well as COVID-19 teacher grants

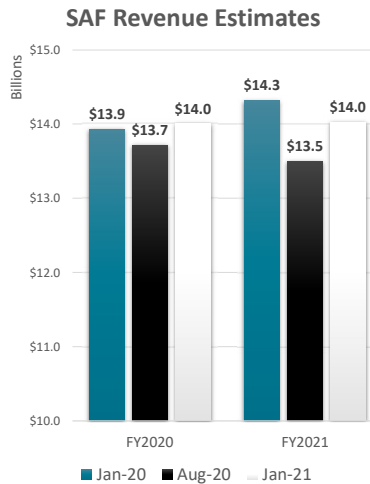
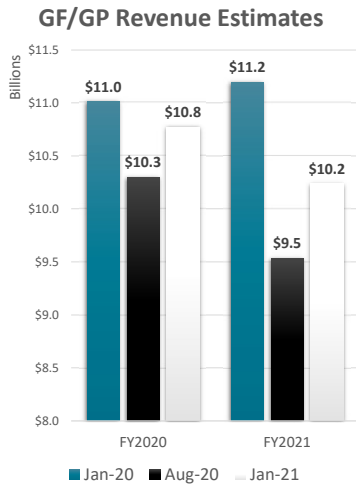


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## January Consensus: Revenue Picture Improves Again



Once again, revenue projections are revised upward.

GF/GP revenue projections increase by \$758M

SAF revenue estimate are up \$1.2B

Source: January 2021 CREC Final Summary.

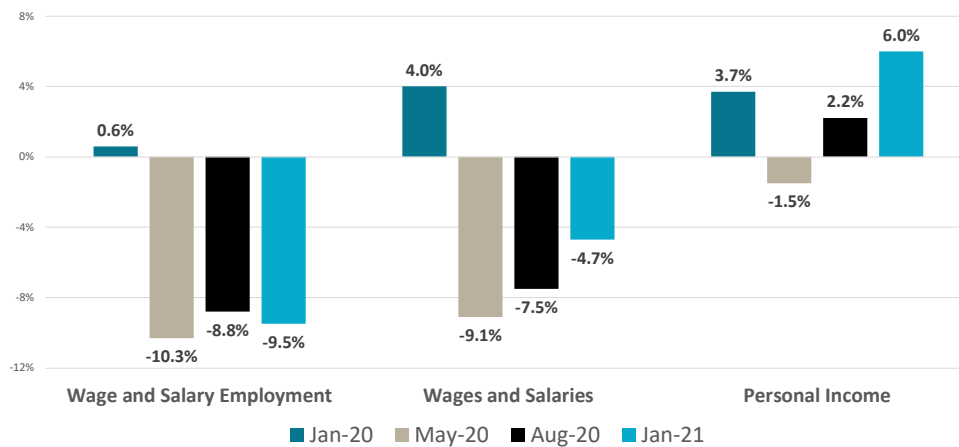


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## What Happened with the Economy?

### Change from CY2019 to CY2020



Source: CREC Final Summaries.

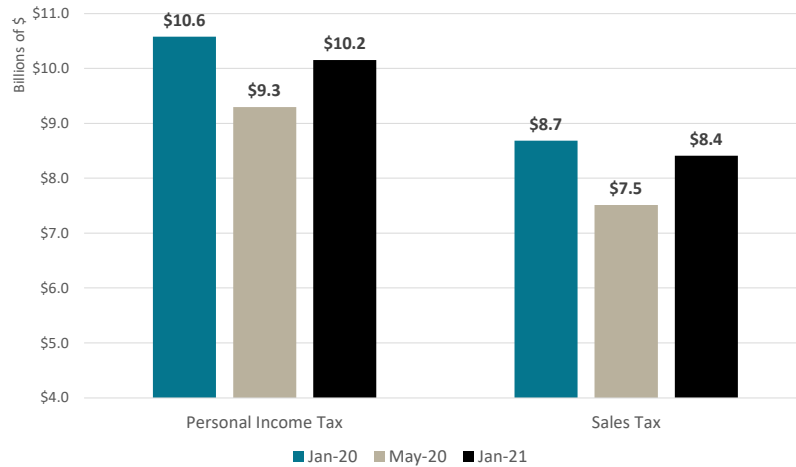


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## What Happened with Revenues?

FY20 Revenue Forecasts for Income and Sales Tax



Source: CREC Final Summaries.

### Key Factors in Mitigating Revenue Loss:

- Enhanced federal unemployment benefits
- Paycheck Protection Program
- Federal tax credit stimulus checks
- Gradual re-opening of portions of economy

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## FY2022 Executive Budget Proposal

Large Fund Balances Drive Significant One-Time Investments

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## Implications for FY2022 Budget

*Unanticipated Revenue Results in Large Fund Surpluses*

Estimated FY2020 Year-End Fund Balances (in millions)	
GF/GP	School Aid Fund
<b>\$2,364.2</b>	<b>\$1,151.6</b>

- Combined \$3.5B in fund balances will be carried into FY2021
- In addition, additional FY2021 savings of \$715M GF/GP are expected per guidance from the Biden administration that enhanced Medicaid match should continue through the end of calendar year 2021

## FY2021 Supplemental Proposals

- Governor proposes to tap into available fund balances to finance a number of major one-time investment proposals outlined in four FY2021 supplemental appropriation requests
- Major funding proposals include:
  - \$2.5B in federal, GF/GP, and School Aid Fund dollars to address learning loss during the pandemic, summer learning programs, and student support services as well as federally-mandated maintenance of efforts payments to universities and community colleges
  - \$4.2B to recognize various federal categorical grants supporting the state's COVID-19 response
  - \$225M GF/GP for grants and capital access program for businesses negatively impacted by the pandemic
  - \$300M GF/GP for a Local Bridge Bundling Initiative

## Governor's FY2022 Budget Recommendation

*in Millions of \$*

	FY2021 Current	FY2022 Executive Budget	% Chg
<b>Total Appropriations</b>	<b>\$61,933.3</b>	<b>\$65,844.9</b>	<b>6.4%</b>
Federal Revenue	\$25,825.7	\$28,358.3	9.8%
General Fund/General Purpose Revenue	\$10,845.5	\$11,403.6	5.1%
School Aid Fund Revenue	\$14,213.2	\$14,714.6	4.0%
Other Revenue Sources	\$11,108.4	\$11,408.4	2.7%

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## Summary of Major Changes – GF/GP and SAF

*Revenue*

	GF/GP (millions)	SAF (millions)
<b>FY2021 Ongoing Appropriations</b>	<b>\$10,316.9</b>	<b>\$14,213.2</b>
New Ongoing Investments	\$193.7	\$252.7
New One-Time Investments	\$592.6	\$266.5
Baseline Adjustments (caseloads, financing, mandates)	\$320.3	\$12.4
Budget Reductions	(\$19.9)	(\$30.2)
<b>FY2022 Executive Budget Recommendation</b>	<b>\$11,403.6</b>	<b>\$14,714.6</b>

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# Education Highlights

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## Recap: COVID Impact on Education Budgets

*Despite revenue uncertainty, FY2020 funding levels increased*

- State appropriations for K-12, higher education, and community colleges protected in FY2020 budget balancing, instead:
  - Federal funding replaced state funding in education budgets - \$712M
  - Rainy Day Fund/GF transfers to School Aid Fund - \$392M
  - On-going appropriations (e.g. foundation grant, university and college operations) see small increases
  - Result: large budget surpluses in GF and SAF
- FY2021 education budgets – flat funding at current service baseline
  - School Aid: replace federal funds with state dollars, one-time \$65 per-pupil payment, \$66M for declining enrollment
  - No on-going operational funding increases for K-12 schools, colleges and universities

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## Supplemental Spending Debate

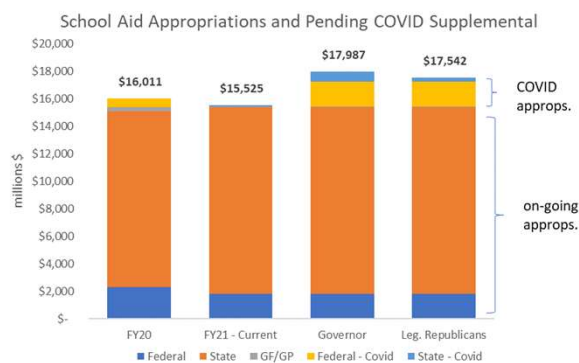
### *COVID-19 funding for K-12 Schools*

- December federal education relief (CRRSA)- add'l \$1.8B for Michigan, includes:
  - \$1.5B directly to districts (traditional and charter) based on federal formula and \$87M for non-public schools
  - Two pots of discretionary funding available to state total \$205M
  - Both sources (formula and discretionary funds) tied up in competing supplemental appropriation proposals
- State funding to address school needs – Governor vs. Leg. Republicans
- RIGHT NOW - schools are pulling together plans for re-opening this spring, as well as summer programming to address learning delays
- Additionally, schools are budgeting for next fall
- Federal and state funding will play a large role in both discussions

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## FY2021 Supplemental Proposals Vary Considerably

### *Mix of federal and state funding – formula and discretionary*



- Governor - \$2.4B
  - Appropriates all available federal funding
  - \$1.6B fed. – thru Title IA formula direct to districts; private school allocation
  - Add'l \$190M fed. and \$610M state – various discretionary allocations for pandemic learning, student recovery, and out-of-school programs
- Legislative Republicans - \$1.9B
  - All available federal funding
  - \$1.6B fed. – thru Title IA formula direct to districts; private school allocation
  - \$840M of total tie-barred to HB4049
  - Add'l \$200M fed. and \$170M state – discretionary allocations: 1) equalize district Title IA allocations (\$450 per-student), 2) student recovery and out-of-school programs

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## Biden Plan Provides Another \$3.9B to Schools

### *Brings Michigan's share of three relief packages to \$6.2B*

- President Biden's \$1.9T American Rescue Plan expected to be signed into law by end of March, includes more K-12 education funding
  - Third package for public schools in less than a year
  - Total: \$6.2B additional funding injected into K-12 schools in short-term
  - Nearly 90% (\$5.4B) – federal formula driven
  - During last recession MI used \$1.5B in federal relief funds for local schools; mostly to back-fill state revenue declines
- Challenges with federal funding
  - Nearly all money allocated to states and districts directly – Title IA formula (90%)
  - Formula results in wide differences in per-student allocations across districts
  - States have limited control over formula funds, but there is a LOT of discretionary money ~\$700M across all three relief packages
  - Few restrictions on how states program these dollars; competing proposals for use of these funds

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## Massive Funding Disparities Result from Formula

### *State can play a role in filling funding gaps*

- Title IA is not designed to align resources to student pandemic learning demands
- ALL students and districts affected by learning disruptions
- Formula does not guarantee each student a base amount of funding
- Per-pupil allocations vary significantly because of design of Title IA formula:
  - Median district ~ \$3,400 per pupil (across all three federal packages)
  - 100 districts receive less than \$1,000 per student
  - Flint ~ \$42,000 per pupil (\$158M total) – more than two times district's annual budget
  - Detroit Public Schools Community District ~ 25% of total Title IA pot (\$27,000 per pupil)
- Wide funding variances also show up among similar, neighboring schools
- State should use state and federal discretionary resources to ensure ALL students receive a base amount of funding (horizontal equity)

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## Take a Step Back

### *Largest investment in K-12 education ever*

- Massive scale of federal funding
  - \$6.2B represents about one-third of total annual K-12 outlays (\$18B)
  - Spread over four years, additional \$1.5B annually
- For handful of districts, represents transformative funding amounts
  - Leverage funding to address student learning needs beyond the pandemic
- District spending decisions – mix of new staff, contractors, facilities
  - How will increased demand for school personnel interact with existing staff shortages?
- State and districts should keep powder dry and pause plans for major investments until federal funding impacts and unmet needs clearer
  - Equalizing per-student allotments should be priority
- Although one-time money, it will prop up district budgets for years

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## Federal K-12 Relief Spending Stretches Out

### *60% estimated to be spent after FY2022*

Estimated Spending Schedules for Various Federal K-12 Education Relief Packages (millions \$)

	Total Allocated	FY20	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
CARES Act	\$ 479.2	\$ 62.3	\$ 215.6	\$ 153.3	\$ 31.1	\$ 15.3	\$ 1.4			
Cons. Approp. - FY21	\$ 1,782.0		\$ 356.4	\$ 534.6	\$ 481.1	\$ 267.3	\$ 89.1	\$ 35.6	\$ 17.8	
Pres. Biden Proposal	\$ 3,870.0		\$ 193.5	\$ 967.5	\$ 967.5	\$ 774.0	\$ 580.5	\$ 270.9	\$ 77.4	\$ 38.7
<b>Total Expenditures</b>	<b>\$ 6,131.2</b>	<b>\$ 62.3</b>	<b>\$ 765.5</b>	<b>\$ 1,655.4</b>	<b>\$ 1,479.8</b>	<b>\$ 1,056.6</b>	<b>\$ 671.0</b>	<b>\$ 306.5</b>	<b>\$ 95.2</b>	<b>\$ 38.7</b>
% of total		1%	12%	27%	24%	17%	11%	5%	2%	1%

Source: Congressional Budget Office

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## Governor's FY2022 Recommendation

*K-12 schools, colleges, and universities modest increases*

### FY2022 recommended education budgets, generally:

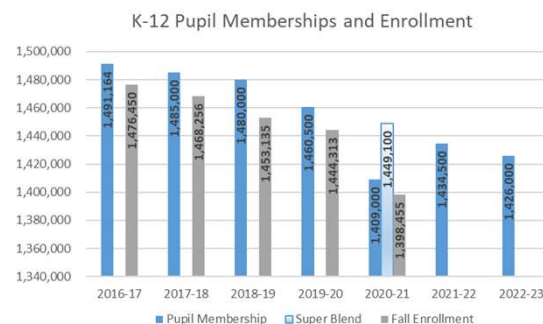
- ~2% increase for operational costs across all budgets; recall higher ed. and colleges did not see funding bumps in FY2021
  - K-12 increase built into foundation; colleges and university funding is one time
- Teacher retirement system payments - \$150M increase (\$1.8B total)
  - These are costs associated with recent reform efforts
- Few specific COVID-related appropriations, state or federal, proposed
  - One source of friction between the Governor and legislature
  - Next round of federal relief around the corner
- Governor recommending handful of major program expansions within School Aid budget

## FY2022 School Aid Highlights

*Overall K-12 spending continues to rise - \$15.8B*

### K-12 Operational Funding

- Per-pupil grant increase – \$82 (1%) to \$164 (2%)
  - Reduces gap in base and target grant to \$336 per student
- Cut cyber school per-pupil grants by 20%
- Second year of declining enrollment support for districts
  - Fall 2020 enrollment in early grades down – 14K fewer kindergarten students
  - Pupil estimates suggest that 5K students from fall 2019 no longer enrolled
  - FY2021 – super blend used for membership count to shield districts from fiscal hit
  - FY2022 – return to 90/10 blend + reimbursement
  - Districts reimbursed for 70% of enrollment loss in FY2021 (but at FY2022 per-pupil amount)



Source: MI School Data, Senate Fiscal Agency

## Other School Aid Highlights

- Modest funding increase (2.5%) in at-risk funding; more closely align with school adequacy study recommendations
- Maintains add'l state special education reimbursement payments above *Durant* minimum %
- Large increase (14%) per-pupil reimbursement rate for Great Start slots – align full day rate with minimum K-12 foundation (\$8,275)
- One-time grant funding for public school drinking water fixture replacements (FY2021 item)

## Looking Forward – School Finance Big Picture

*Federal relief layered on growing state spending base*

- Federal education relief funding large part of school district finance discussions over coming years
  - \$2.3B received thus far; it will take time to spend down these resources
  - Another \$3.9B around the corner; stretches out federal spend
- Meanwhile - K-12 state funding continues to rise at modest clip
- Do districts face the prospect of a fiscal cliff?
  - Not like Great Recession – SAF revenue healthy and state appropriations increasing
  - Education funding, particularly K-12, held harmless from major cuts
  - Federal dollars **NOT** replacing state funds – all **NEW** spending
  - Gradual “off ramp”; federal COVID spending peaks in FY2022 (\$1.7B) and falls to \$1.5B in FY2023
- State should monitor how the federal investment is meeting students’ needs during and after pandemic; where it is falling short, allocate limited state dollars to address funding gaps

# Other Budget Highlights

Major One-Time Investments Draw Down GF/GP Balance



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## January Supplemental: COVID-19 Response

Governor's requests FY2021 supplemental in January to recognize newly available federal support arising from December federal stimulus bill

- Emergency rental and utility assistance: \$661M
- COVID testing and contact tracing: \$575M
- COVID vaccination efforts: \$90M
- Enhanced food assistance benefits: \$2.1B

Legislative plan passed by the Senate on Tuesday holds back some funding and places a number of conditions on expenditures

- Earmarks: federal testing funds to K-12 schools (\$37.5M), prisons (\$20M), skilled nursing facilities (\$25M); federal vaccination funds to health providers and local public health departments (\$36.7M)
- Appropriates \$347M of testing dollars as contingent fund requiring enactment of Senate Bill 1 (which limits the validity of epidemic-related emergency orders to 28 day without legislative approval for an extension)
- Appropriates \$110M for vaccination efforts as a reserve fund and conditions expenditures on additional legislative approvals and the submission of spend plan details



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## January Supplemental: Small Business Support

Governor's recommends \$235 million GF/GP to support grants and capital access programs aimed at businesses that have experienced losses and financial strain during the pandemic

- \$125M for Main Street Recovery Initiative
  - Grants up to \$20,000 and low-interest capital
  - Targets small businesses with 25 or fewer employees)
- \$75M for a Business Accelerator and Resiliency Initiative
  - Grants up to \$100,000 for eligible businesses for operating capital
  - Special focus on high-tech start-up companies
- \$25M for a Microenterprise Support Initiative
  - Grants up to \$35,000 and support services to businesses
  - Targets very small businesses with 9 or fewer employees
- \$10M to support the safe re-opening of restaurants

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## Legislative Response: Tax and Fee Relief

Legislative supplemental scraps Governor's business support proposal and recommends \$405 million GF/GP to grants to nine categories of "afflicted businesses.

- \$300M for Property Tax relief grants – capped at 2020 payment level
- \$55M for Unemployment Insurance relief grants – capped at 50% of taxes paid during the previous four quarters
- \$16.5M for Liquor License Fee relief – capped at 2020 liquor license fees paid by licensed retail liquor establishments
- \$22M for Food Service Establishment relief - capped at 2020 license and inspection fees paid
- \$11.5M for License and Inspection Fee relief – capped at 2020 license and inspection fees paid by establishments in selected entertainment, hospitality, and service industries
- Grant generally paid on sliding scale based on demonstrated loss in gross receipts of at least 5% in a 2020 calendar quarter over the same 2019 period
- Legislative plan also includes \$150M GF/GP deposit into the Unemployment Insurance Trust Fund

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## Direct Care Worker Wage Support

Governor and Legislature have alternative plans for extending the \$2/hour wage increase for direct care workers first initiated on a temporary basis in April 2020 and extended through February 2021.

Key Provisions	Governor	Legislature
Wage increase and eligibility	<b>\$2.00/hour applied to current recipients:</b> <ul style="list-style-type: none"> <li>• Medicaid behavioral health services</li> <li>• Care in skilled nursing facilities</li> <li>• Community-based supports (e.g. MiChoice, adult home help)</li> <li>• In-homes care services through Area Agencies on Aging</li> </ul>	<b>\$2.25/hour to current recipients and expanded starting 3/1/21 to services in:</b> <ul style="list-style-type: none"> <li>• Adult foster care</li> <li>• Homes for the Aged</li> <li>• Direct support/job coaches within Supported Employment Arrangements</li> </ul>
Duration of wage increase	Proposes permanent increase with full-year funding in FY2022 budget	Supplemental extends increase through 9/30/21; TBD on FY2022
New proposals		Temporary \$2.00/hour increase from 3/1/21 to 6/30/21 for: <ul style="list-style-type: none"> <li>• Frontline workers in residential child caring institutions</li> </ul>
Funding	<b>FY2021: \$110 million (\$43.1 million GF)</b> <b>FY2022: \$360 million (\$121.4 million GF)</b>	<b>FY2021: \$150 million (\$55 million GF)</b>

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## Local Bridge Bundling Initiative

Governor's FY2021 supplemental recommendations include \$300M in one-time GF/GP funding to repair or replace 120 local bridges in serious or critical condition

- Priority given to bridges closed to local traffic, those with restrictions to state load limitations, and those identified by Regional Bridge Councils as being critical to public safety and commercial traffic
- Timeline: RFPs developed and issued in fall 2021; construction worked targeted for spring 2022
- Initiative builds on existing federally-funded pilot program; statewide "bundling" approach is expected to result in cost savings related to design, contracting, and construction
- Over 1,000 local bridges were rated as being in poor, serious or critical condition as of November 2018

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## Expanded Child Care Support

Executive Budget would expand eligibility for child care subsidies and day care provider reimbursement under the state's subsidy program

- Between April 1, 2020 through September 30, 2022:
  - Income eligibility for subsidies increases from 150% to 200% of the federal poverty level (FPL); following this period, eligibility moves to 160% of FPL
  - State covers family co-pays that traditionally apply within the program
- Child care provider reimbursement rates increase by 10%
- Between April 1, 2020 and December 31, 2020, providers are paid based on enrollment rather than actual daily attendance
- \$55 million in one-time funding is provided for Business Support Grants to help child care providers remain open during the pandemic
- Funding: **\$292.1M** in federal stimulus funding in FY2021 supplemental combined with **\$78M** in one-time GF/GP funding in FY2022

## Is More Federal Stimulus Coming?

- U.S. House Coronavirus relief bill passed last Friday includes \$350 billion for State and Local Fiscal Relief
- Looser restrictions on usage of funds than previous CRF allocation
  - Respond to or mitigate COVID-19 public health emergency or its negative economic impacts
  - Cover costs incurred as a result of COVID-19 emergency
  - Replace lost revenue from January 2020 projections
  - Address the negative economic impacts of the COVID-19 emergency
- Estimated Allocations (Federal Funds Information for States):
  - State of Michigan: \$5.7B
  - Michigan counties and municipalities: \$4.4B

# Looking Ahead to FY2023

Structural Budget Imbalance Results in Shortfalls



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## GF/GP Shortfall Likely in FY2023

### GF/GP Balance Sheet Projections (\$ in millions)

	<u>FY22</u>	<u>FY23</u>
<b>Beginning Balance</b>	<b>\$1,005.6</b>	<b>\$61.7</b>
Revenue Estimate	\$10,897.1	\$11,167.1
Revenue Adjustments	(\$434.4)	(\$422.0)
<b>Ongoing Revenue</b>	<b>\$10,462.7</b>	<b>\$10,745.1</b>
Ongoing Appropriations	\$10,815.0	\$10,815.0
One-Time Appropriations	\$591.6	
FY23 Cost Pressures		\$370.0
<b>Estimated Expenditures</b>	<b>\$11,406.6</b>	<b>\$11,185.0</b>
<b>Ending Balance</b>	<b>\$61.7</b>	<b>(\$378.2)</b>

- FY2022 expenditures exceed available revenue, reducing year-end balance to just \$61.7 million
- FY2023 cost pressures include loss of GF/GP savings from enhanced FMAP, other baseline adjustments, and state payroll costs
- Assumes no continuation of FY2022 one-time investments

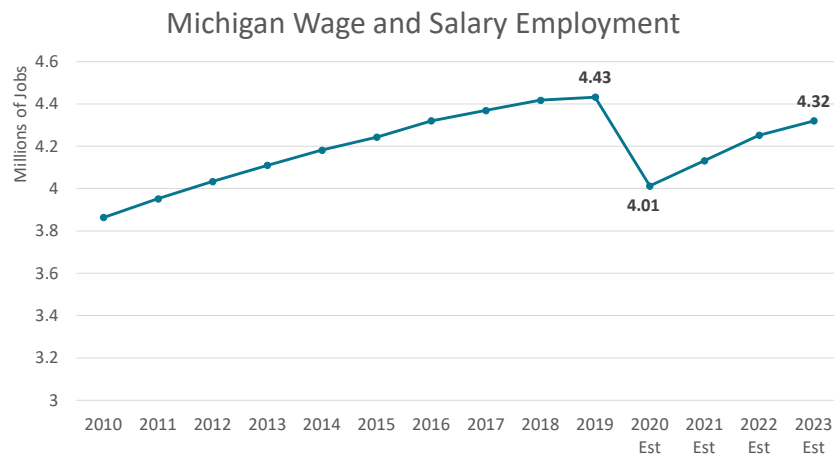


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## Employment Growth Remains Sluggish

Employment remains below pre-pandemic level into FY2023 under current economic forecasts



Source: House Fiscal Agency



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## When Does the Pandemic End?

- Current long-term outlook suggests small structural GF/GP shortfall, but uncertainty remains about pandemic and economy
- State revenues losses largely mitigated by pandemic federal stimulus – but how quickly does economy return to normal?
- Current surplus and pending stimulus dollars: spend it or save it?



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