



Analyzing the
Governor's FY22 Budget
Recommendation

Analyzing the Governor's FY22 Budget Recommendation

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Revisiting 2020: Impact of COVID-19 on the State Budget

Onset of COVID-19 in 2020

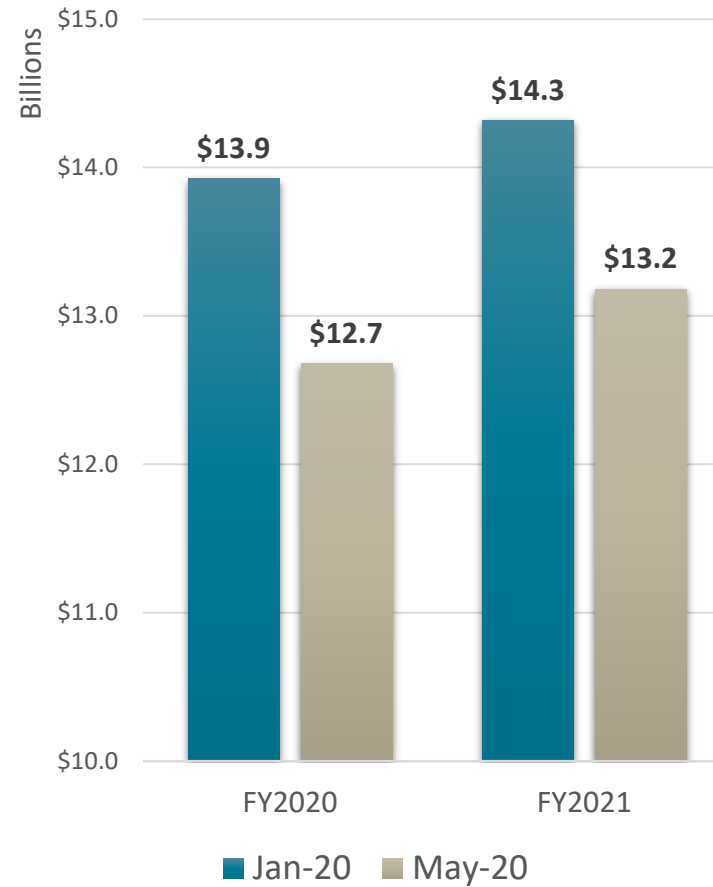
- February 6: FY21 Executive Budget proposal is released; no funding specific to COVID-19
- March 10: MIRS News – Governor confirms first two “presumed positive” Coronavirus cases in Michigan and declares state of emergency; 63 Michiganders tested; 124 under active monitoring
- Executive Orders and Developments
 - 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, etc

Revenue Estimates Plummet in May

GF/GP Revenue Estimates



SAF Revenue Estimates



May 2020: Combined GF/GP and School Aid Fund (SAF) revenue projections down \$6.3B

FY20 revenue forecast down \$3.2M, necessitating budget reductions more than mid-way through the fiscal year

Source: May 2020 CREC Final Summary.

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
 - Federal law limited use of funding to COVID response activities; no flexible funding for states to address declining revenues
 - Eventual guidance – CRF funding can be used for general activities that have been substantially diverted to COVID-19 response
- Enhanced Medicaid match: federal share of state Medicaid spending goes up 6.2% retroactive to January 1, 2020

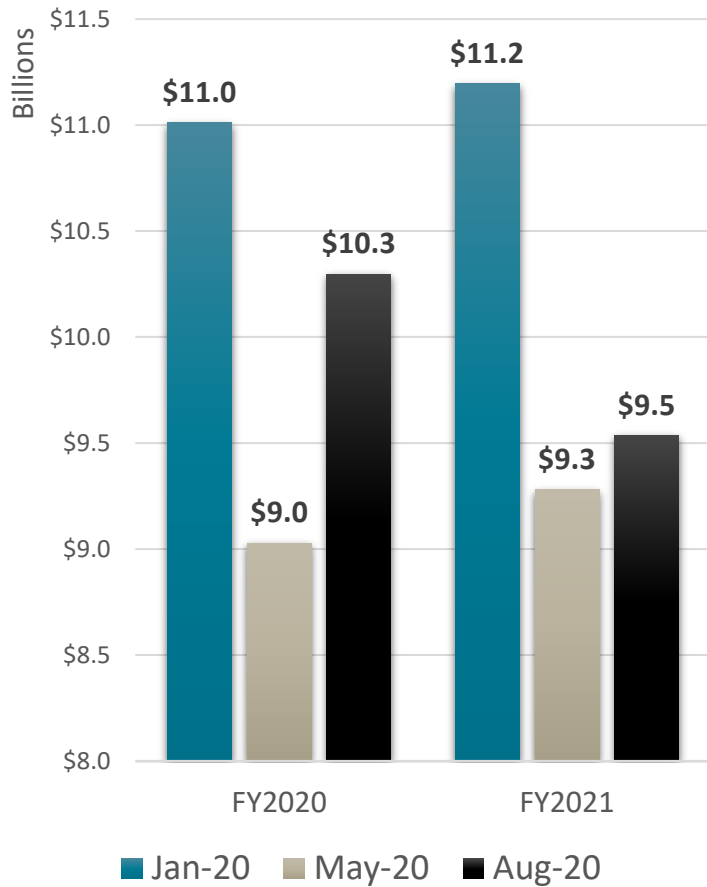
Rewriting the FY20 Budget

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

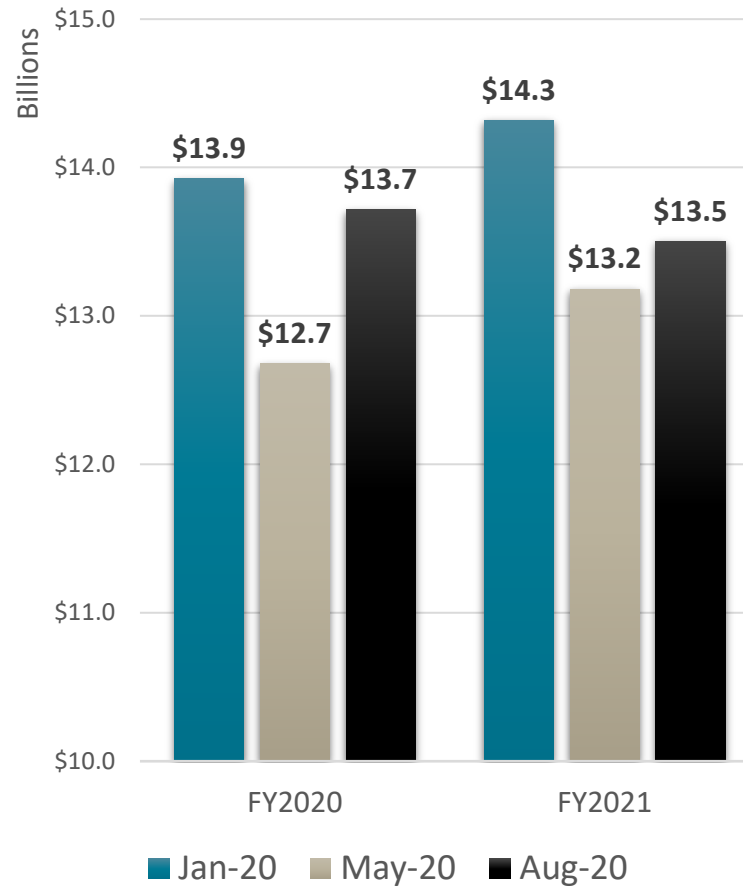
Budget/Revenue Savings	GF/GP (millions)	SAF (millions)
Federal CRF offsets state costs (Public Safety staff, K-12, Higher Education, Revenue Sharing, COVID Response)	\$696.5	\$456.0
Enhanced Federal Medicaid Match: applied Jan-Sep 2020	\$523.3	
Budget Stabilization Fund Deposit into School Aid Fund		\$350.0
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
Savings for Fund Balances	\$1,293.4	\$1,181.1

Revenue Picture Greatly Improves in August

GF/GP Revenue Estimates



SAF Revenue Estimates



After finalizing the FY 20 budget, FY20 revenues were revised up by \$2.3B across both major funds.

FY21 estimates up a combined \$500M.

Source: August 2020 CREC Final Summary.

Finalizing the FY21 Budget

Improving Revenue Picture Largely Eliminates Remaining Shortfall

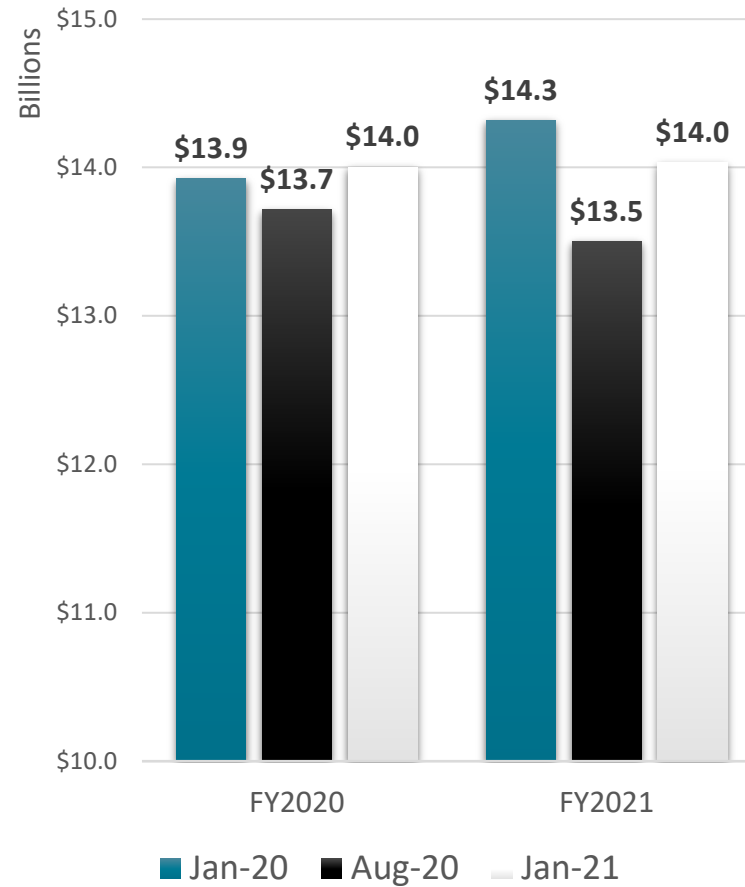
- School Aid Fund surplus: \$355 million
 - Increase for K-12 schools and Community Colleges: \$187M
 - Remaining SAF balance is used to reduce GF/GP support by \$169M
- General Fund shortfall: \$502 million
 - Enhanced Medicaid match extended to first quarter FY21: \$240M
 - Additional CRF to offset GF/GP: \$146M
 - 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

January Consensus: Revenue Picture Improves Again

GF/GP Revenue Estimates



SAF Revenue Estimates



Once again, revenue projections are revised upward.

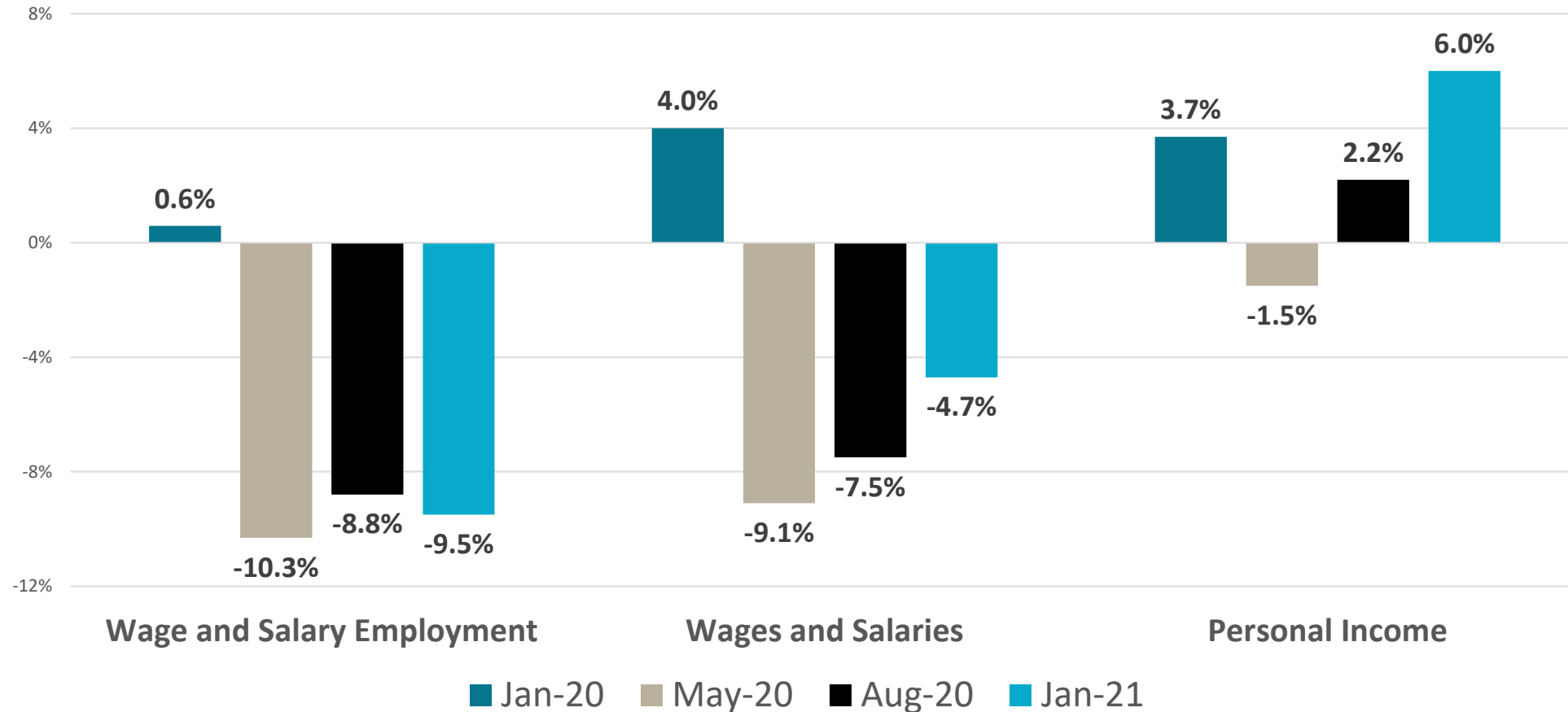
GF/GP revenue projections increase by \$758M

SAF revenue estimate are up \$1.2B

Source: January 2021 CREC Final Summary.

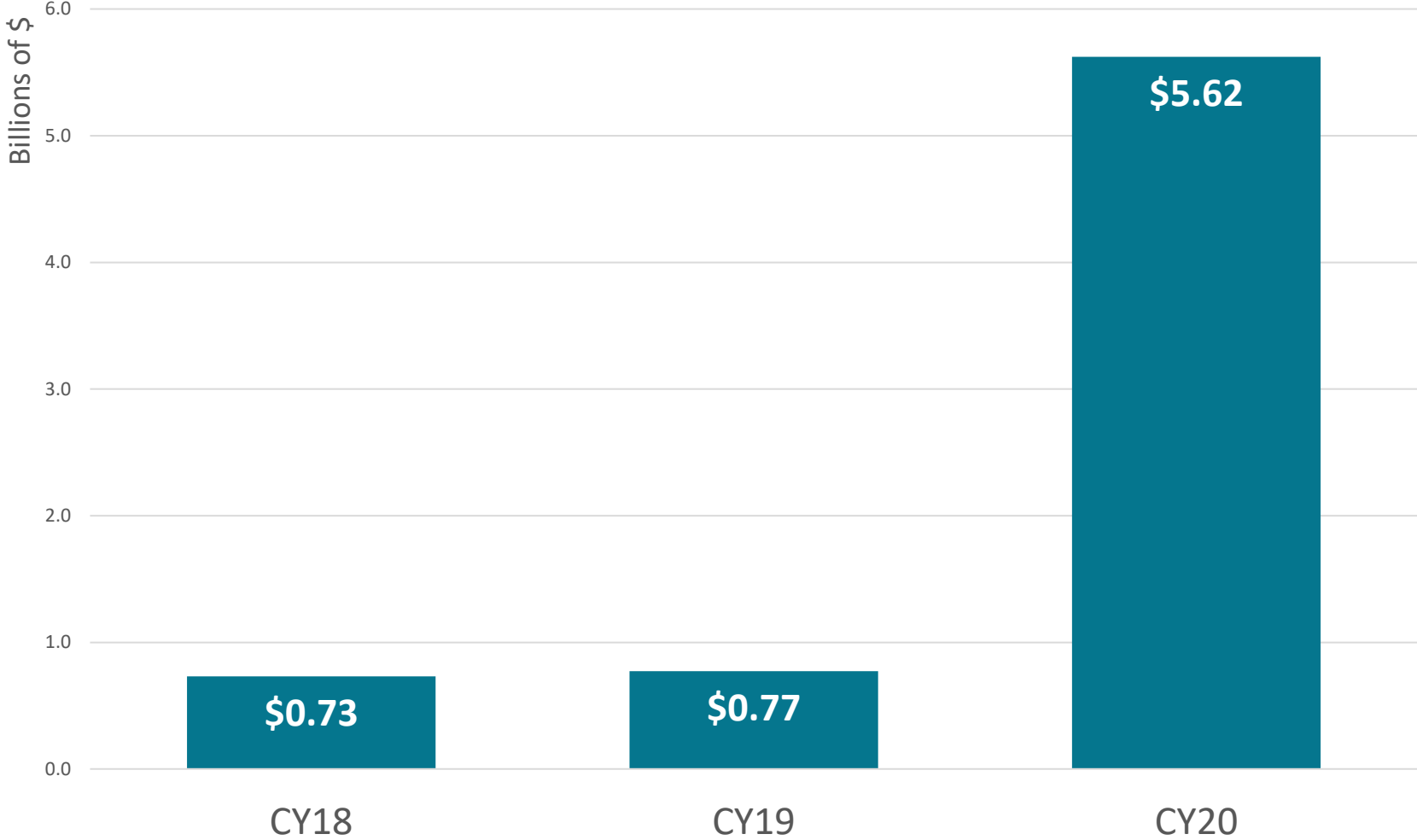
What Happened with the Economy?

Change from CY2019 to CY2020



Source: CREC Final Summaries.

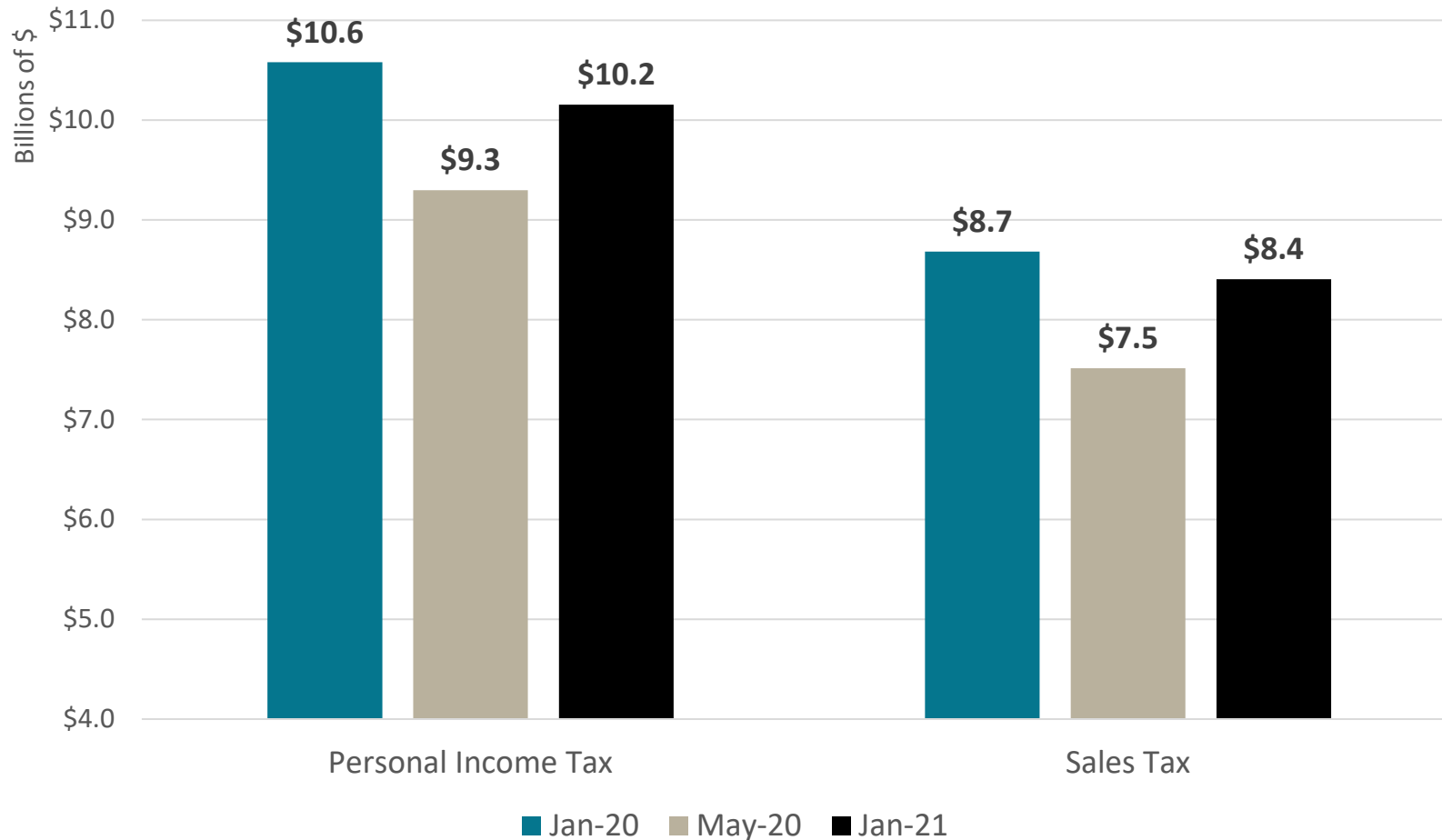
Large Increase in Unemployment Benefits in 2020



Source: U.S. Department of Labor data.

What Happened with Revenues?

FY20 Revenue Forecasts for Income and Sales Tax



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

Source: CREC Final Summaries.

FY22 Executive Budget Proposal

Large Fund Balances Drive Significant One-Time Investments

Implications for FY22 Budget

Unanticipated Revenue Results in Large Fund Surpluses

Estimated FY20 Year-End Fund Balances (in millions)	
GF/GP	School Aid Fund
\$2,364.2	\$1,151.6

- Combined \$3.5B in fund balances will be carried into FY21
- Additional FY21 DHHS caseload savings of \$715M GF/GP; guidance from the Biden administration that enhanced Medicaid match should continue through the end of calendar year 2021
- Governor proposes to draw on these balances to fund major one-time investments contained in FY21 supplemental requests

Governor's FY22 Budget Recommendation

in Millions of \$

	FY21 Current	FY22 Executive Budget	% Chg
Total Appropriations	\$61,933.3	\$65,844.9	6.4%
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%

Summary of Major Changes – GF/GP and SAF

Revenue

	GF/GP (millions)	SAF (millions)
FY21 Ongoing Appropriations	\$10,316.9	\$14,213.2
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)
FY22 Executive Budget Recommendation	\$11,403.6	\$14,714.6

Education Highlights

Recap: COVID Impact on Education Budgets

Despite revenue uncertainty, FY20 funding levels increased

- State appropriations for K-12, higher education, and community colleges protected in FY20 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
- FY21 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

Supplemental Spending Debate

COVID-19 funding for K-12 Schools

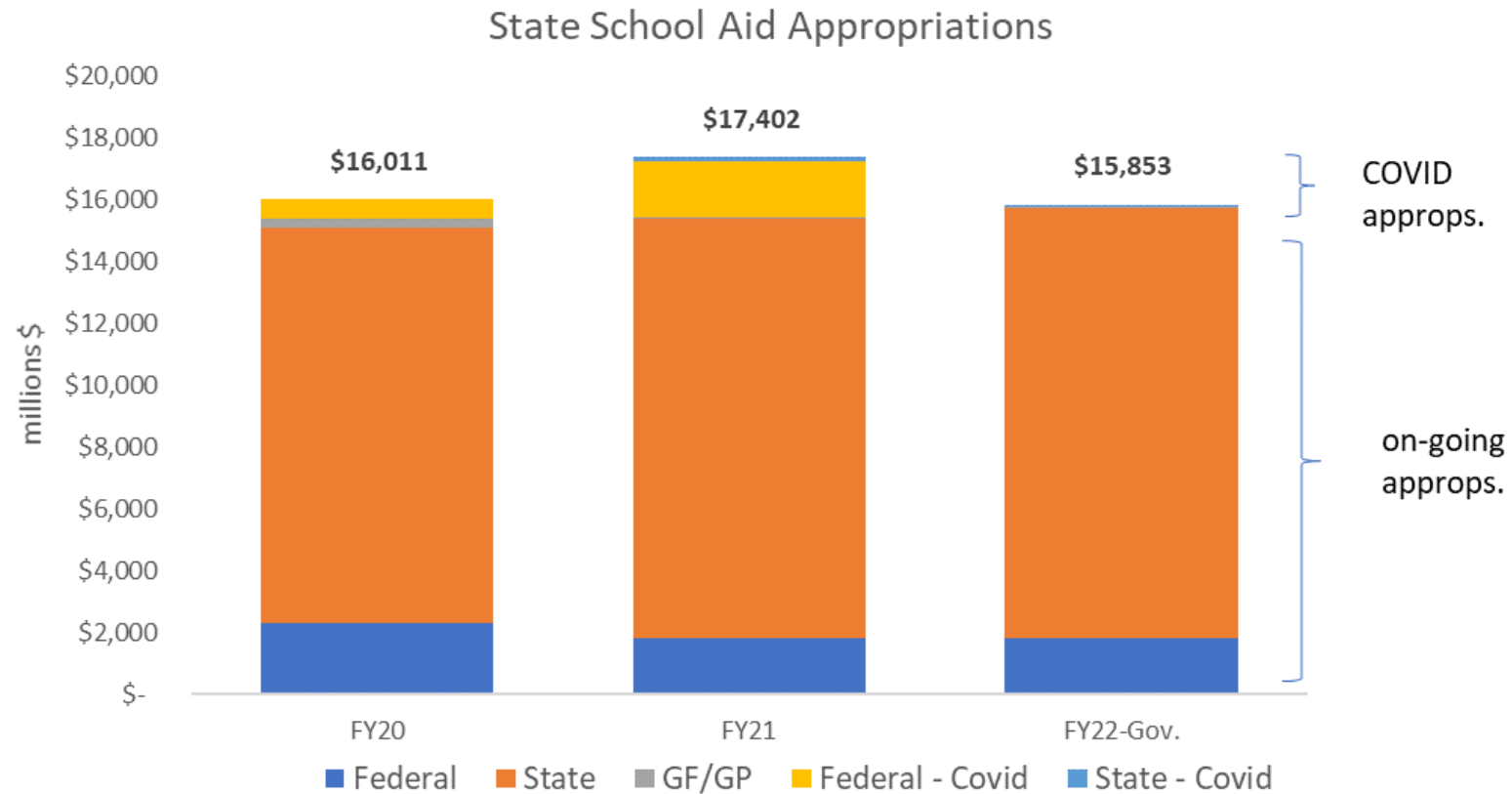
- December federal education relief (CRRSA)- add'l \$1.8B for Michigan, includes:
 - \$1.5B directly to districts (traditional and charter) based on federal formula and \$87M for non-public schools
 - Two pots of discretionary funding available to state total \$205M
 - Both sources (formula and discretionary funds) tied up in competing supplemental appropriation proposals
- 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

Supplemental – what made the cut

Federal funding and vetoes

- Final product reflects legislative priorities
- \$1.5B federal direct to districts through Title IA
 - \$841M of total conditioned on passage a bill limiting governor's power
 - Governor's veto of HB4049 could hold up the release of federal funds
- Discretionary federal dollars (\$200M): student recovery, mental health and out-of-school programs, staffing incentives
- \$136M to equalize per-pupil funding allocations (Title IA)
- Veto: \$90M in private school funding

School Aid Budget Swells with influx of federal dollars



Source: Citizens Research Council

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

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)

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

Federal K-12 Relief Spending Stretches Out

60% estimated to be spent after FY22

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
Total Expenditures	\$ 6,131.2	\$ 62.3	\$ 765.5	\$ 1,655.4	\$ 1,479.8	\$ 1,056.6	\$ 671.0	\$ 306.5	\$ 95.2	\$ 38.7
% of total		1%	12%	27%	24%	17%	11%	5%	2%	1%

Source: Congressional Budget Office

Governor's FY22 Recommendation

K-12 schools, colleges, and universities modest increases

FY22 recommended education budgets, generally:

- ~2% increase for operational costs across all budgets; recall higher ed. and colleges did not see funding bumps in FY21
 - 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

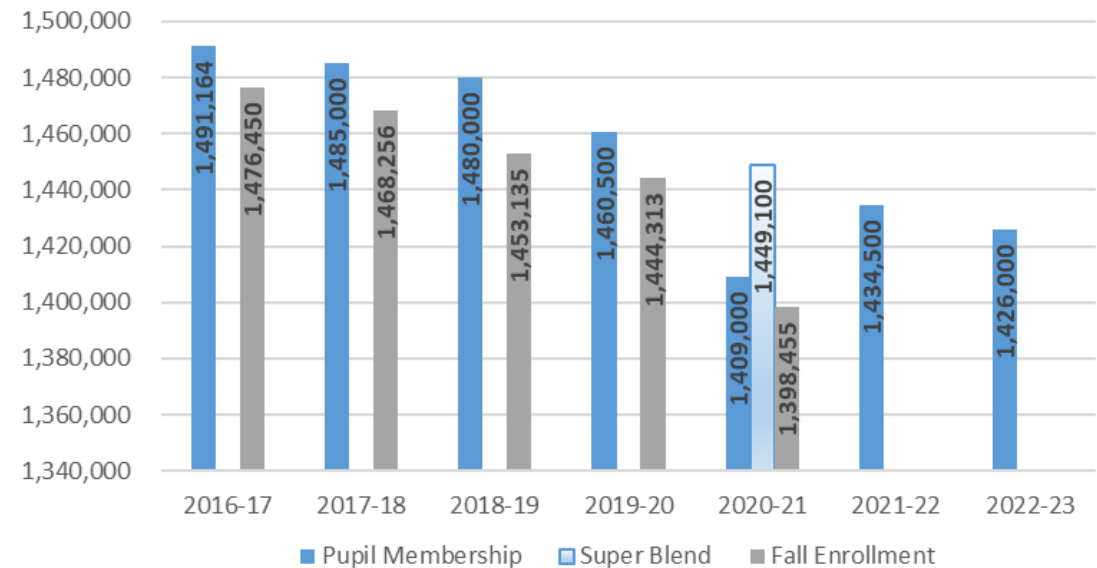
FY22 School Aid Highlights

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
 - FY21 – super blend used for membership count to shield districts from fiscal hit
 - FY22 – return to 90/10 blend + reimbursement
 - Districts reimbursed for 70% of enrollment loss in FY21 (but at FY22 per-pupil amount)

K-12 Pupil Memberships and Enrollment



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 (FY21 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 FY22 (\$1.7B) and falls to \$1.5B in FY23
- 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

January Supplemental: Small Business Support

Governor's budget 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
 - Supports small businesses with 25 or fewer employees (grants) or with 50 or fewer employees (capital access)
- \$75M for a Business Accelerator and Resiliency Initiative
 - Grants up to \$100,000 for eligible businesses for operating capital
 - Emphasis 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

Legislative Response: Tax and Fee Relief

Governor vetoed on Wednesday an \$405 million alternative business support plan proposed by the legislature focused on tax and fee relief to “afflicted businesses” in selected sectors of the economy

- \$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
- Governor also vetoed \$150M GF/GP deposit into the Unemployment Insurance Trust Fund

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	<p>\$2.00/hour applied to current recipients:</p> <ul style="list-style-type: none"> • Medicaid behavioral health services • Care in skilled nursing facilities • Community-based supports (e.g. MiChoice, adult home help) • In-homes care services through Area Agencies on Aging 	<p>\$2.25/hour to current recipients and expanded starting 3/1/21 to services in:</p> <ul style="list-style-type: none"> • Adult foster care • Homes for the Aged • Direct support/job coaches within Supported Employment Arrangements
Duration of wage increase	Proposes permanent increase with full-year funding in FY22 budget	Supplemental extends increase through 9/30/21; TBD on FY22
New proposals		<p>Temporary \$2.00/hour increase from 3/1/21 to 6/30/21 for:</p> <ul style="list-style-type: none"> • Frontline workers in residential child caring institutions
Funding	<p>FY21: \$110 million (\$43.1 million GF) FY22: \$360 million (\$121.4 million GF)</p>	FY21: \$150 million (\$55 million GF)

Local Bridge Bundling Initiative

Governor's FY21 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

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 FY21 supplemental combined with **\$78M** in one-time GF/GP funding in FY22

Workforce Development Proposals

Executive recommendation includes one-time to support Michigan Reconnect and Futures for Frontliners initiatives

- Michigan Reconnect: \$120M GF/GP in FY22 budget proposal
 - Targets adults over 25 who have high school diploma but no further education
 - State scholarship covers remaining tuition for 2-year degree program after other financial aid
 - Funding builds on \$60 million in Talent Investment Fund support
 - Funding assumes 80,000 students each year; supports two-year cohorts through FY23
- Future for Frontliners: \$21M for FY21; \$39M for FY22 (all GF/GP)
 - Targets adults over 18 who served as essential frontline workers during the pandemic
 - Programs covers costs of community college programs and high school completion
 - New funding supplements \$15 million in existing federal stimulus support for program
 - Proposed expansion expected to support an additional 22,000 workers
- Additional \$12M in wrap-around supports for participants (e.g., child care, tutoring, career/education counseling)

Looking Ahead

More Federal Stimulus On Its Way

Governor's Budget Draws Down GF Balance

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

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

- FY22 expenditures exceed available revenue, reducing year-end balance to just \$61.7 million
- FY23 cost pressures include loss of GF/GP savings from enhanced FMAP, other baseline adjustments, and state payroll costs
- Assumes no continuation of FY22 one-time investments

More Federal Stimulus is Likely Coming

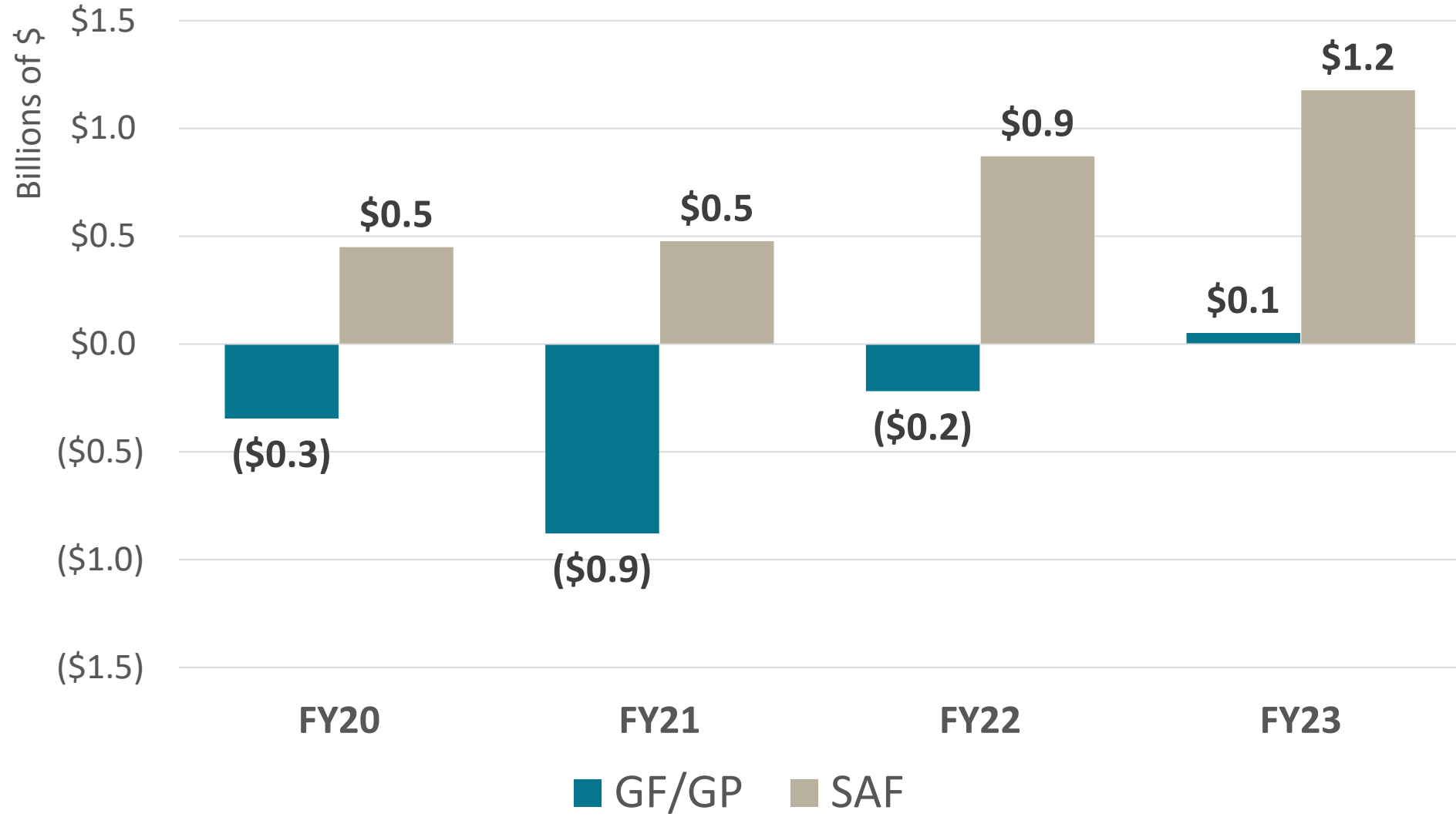
- U.S. House finalized Coronavirus relief bill on Wednesday that includes \$350 billion for State and Local Fiscal Relief
- Funds available until December 31, 2024 to:
 - Respond to COVID-19 public health emergency or its negative economic impacts
 - Provide premium pay up to \$13/hour for workers performing essential work to protect the health and well-being of the public
 - Provide government services to offset the reduction in revenue due to the COVID-19 emergency from the previously completed fiscal year before the pandemic (i.e., FY19)
 - Make necessary investments in water/sewer/broadband infrastructure
 - Prohibitions: can't offset tax cuts; no pension fund deposits

Michigan's Allocation: \$10.3 Billion

- **State of Michigan: \$5.65B**
- **Michigan Counties: \$1.94B**
 - Ingham County: \$56.71M
 - Eaton County: \$21.39M
 - Clinton County: \$15.44M
- **Michigan Municipalities: \$2.47B**
 - City of Detroit: \$879.59M
 - City of Lansing: \$50.99M
 - City of East Lansing: \$12.27M
- **Capital Projects: \$250M available to State of Michigan**

Source: U.S. House Committee on Oversight and Reform, 3/9/21

Estimated Revenues - Change from FY19



Stimulus Exempts UI Benefits from Income Tax

- For tax year 2020, Unemployment Insurance benefits will be partially exempt from federal income taxes to avoid April surprises for recipients; seems to apply to state taxes as well
 - Benefits of up to \$10,200 are tax exempt
 - Applies to persons with Adjusted Gross Income below \$150,000
- Implications for Michigan
 - Withholding alone from UI was \$557 million
 - Estimated that only around half withhold from benefits
 - Many have filed already – amended returns would be needed
 - Impact is uncertain – additional stimulus dollars could be needed to cover revenue loss

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?
- How do you use the new federal stimulus dollars?

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