

SCHOOL EQUITY CAUCUS

Making a difference for the public school children of Michigan

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CAUCUS INFORMATION ALERT

May 19, 2023

Re: Consensus Revenue Estimating Conference

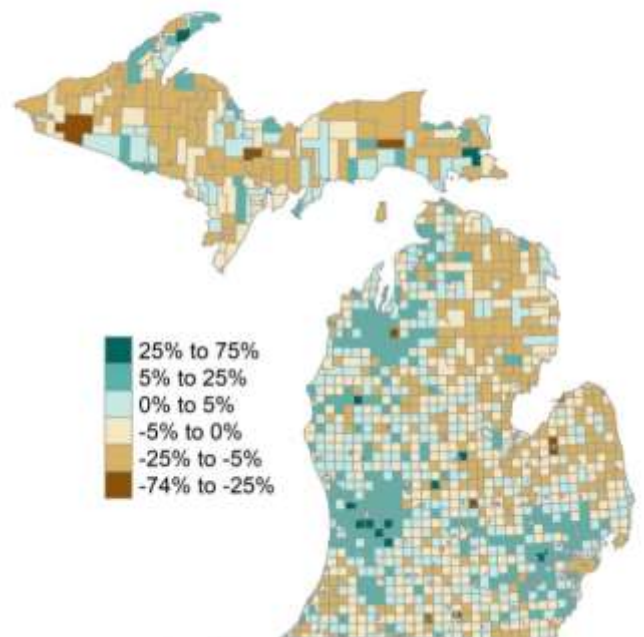
On Friday, representatives of the House and Senate Fiscal Agencies, Treasury, and outside economists met this morning to arrive at “official” revenue estimates for the current and upcoming fiscal years as part of their semi-annual Consensus Revenue Estimating Conference (CREC). Friday’s meeting provided the “final” numbers on which next year’s state budget will be based by providing a snapshot of how revenue in the major state funds is doing to this point in the fiscal year. The previous CREC was held in January.

As part of Friday’s meeting, members of the CREC received updates regarding the economy, both in the US and in Michigan. In general, those reports could be considered to contain cautious optimism moving forward. In the short term, economic growth is expected to slow and cool for the rest of this year (perhaps falling into a mild recession), with a rebound to more normal and stable growth occurring between mid-2024 and early 2025. Inflation is declining somewhat, but wage pressure remains quite high. Employment in Michigan is now nearly back to pre-pandemic levels (US employment hit this level about a year ago). However, Michigan residents lost an average of nearly 10% in their real disposable income (after inflation) over the last year.

The CREC also heard a presentation from the State Demographer regarding Michigan’s demographic trends and their potential impact on the economy. For the first time starting in 2020, Michigan’s deaths have outpaced births meaning that Michigan’s natural population change is now in a net decrease mode. However, the impact of this trend has been blunted by incoming international migration so that the state’s total population has remained relatively flat over the last twenty years. Over the last decade, Michigan’s population growth between 2010 and 2020 was at 2%, while the nation as a whole increased by 7.5%. This left Michigan as 46th in the nation in population growth. The map at right was shared showing areas of population growth or decline in Michigan between 2010 and 2020.

At the same time, over the last twenty years Michigan’s median age has increased by 4.3 years –

Percent Change in Population of Michigan’s Cities and Townships, 2010–2020



Source: 2010 and 2020 PL File, U.S. Census Bureau

the largest increase among Midwestern states. Michigan has moved from being the 29th oldest state in the nation twenty years ago to our current rank as the 14th oldest. As our population ages, this has an impact on the state's labor participation rates (there has been a decline in the percentage of individuals participating in the work force over the last several years) and potentially impacts our ability to support retirees in the long term. In education, we have certainly seen the impact of this demographic trend – both in the number of students served and the difficulty in finding staff. The labor market in Michigan is expected to remain quite tight for the foreseeable future.

Over the last few months, there have obviously been a number of tax rate and policy changes which are impacting the outlook for state revenues. The income tax trigger has reduced the 2023 income tax rate to 4.05% (from 4.25%). On top of that, there has been an unexpectedly large shortfall in income tax revenue since the start of 2023 (about \$450 million short of anticipated levels). On the good side, business income tax collections have been running about \$100 million ahead of projections.

All told it is estimated that the changes in taxes will reduce revenue by more than \$1 billion in the 2022-23 fiscal year, with a reduction of nearly \$2 billion next year and an additional \$1.4 billion in 2024-25. While most of these revenue reductions will impact the state's General Fund (GF/GP), there may well be impacts on the School Aid Fund (SAF) as legislators try to balance the budget. The chart at the right provides the net impacts of all of these changes.

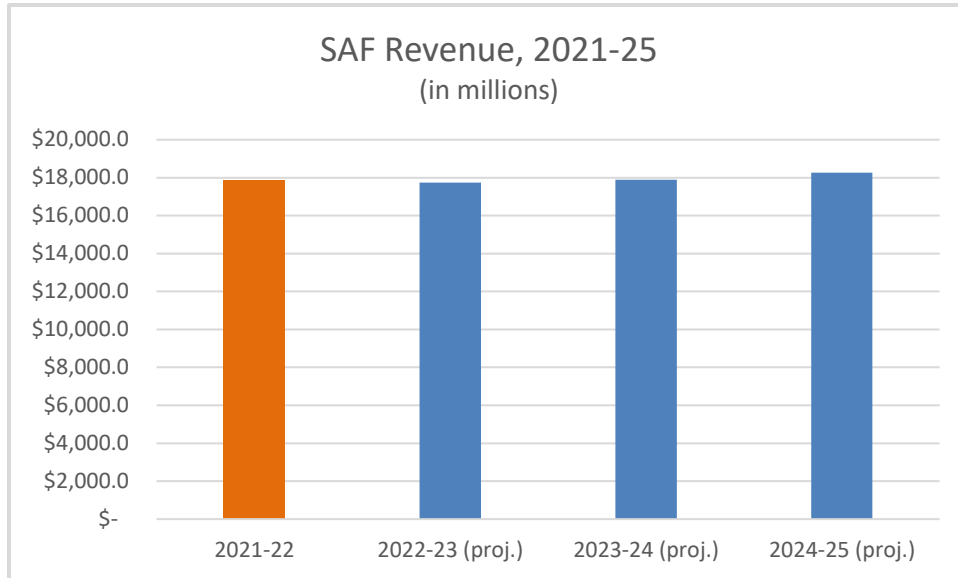
TAX CHANGES IMPACT REVENUE COLLECTIONS
 Legislation enacted since the January conference will lower revenue estimates
 Combined impact will lower GF-GP and SAF Revenue (values in millions):

	FY 2023	FY 2024	FY 2025
Individual Income Tax Rate Trigger	-\$428.2	-\$218.7	
PA 4: Corporate Income Tax Earmarks	-\$600.0	-\$600.0	-\$600.0
PA 4: Earned Income Tax Credit		-\$768.0	-\$384.0
PA 4: Retirement Taxation Changes		-\$281.0	-\$350.0
PA 20, 21, 29: Delivery & Installation Exemption	-\$18.0	-\$62.9	-\$63.8
Total Tax Policy Impacts on Revenue	-\$1,046.2	-\$1,930.6	-\$1,397.8

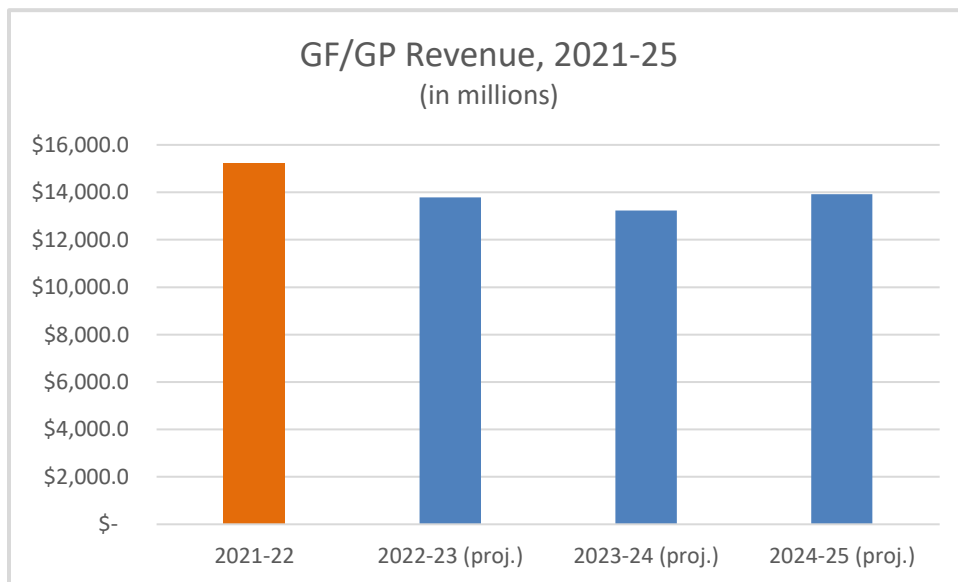
May 2023 Coronavirus Conference

With that as background, here are the official revenue numbers established today...

The state's School Aid Fund (SAF) revenue for the current year is now being projected to decrease by 0.8% (down \$139 million) to \$17.7 billion, an improvement by a little more than \$100 million over what had been projected at the January CREC. In 2023-24 there is expected to be an increase of a similar 0.8% (\$145 million). Therefore, SAF revenue will essentially be flat for 2021-22 through 2023-24, hovering between \$17.7 and \$17.9 billion. In 2024-25 the CREC projections now see SAF revenue increasing by \$377.7 million (2.1%) to \$18.27 billion. These are positive numbers, but are of course not of the same magnitude as the massive increases we have seen in the immediate post-COVID time period. The chart below illustrates this relatively flat revenue pattern.



On the General Fund (GF/GP) side, the results were nowhere near as good. Due in large part to the tax policy changes and lower-than-expected income tax collections described above, 2022-23 revenues are now projected to decrease at a whopping rate of 9.4% (equating to a reduction of more than \$1.4 billion). Looking further ahead, GF/GP revenue is expected to continue declining by a further 4.0% in 2023-24 before recovering some of the losses in 2024-25 (a 5.1% increase from the new lower amount). In real dollar terms, the GF/GP in 2023-24 is expected to generate revenues of \$13.2 billion, a far cry from the \$15.2 billion collected in 2021-22.



It is important to note though that both the SAF and GF/GP had extremely healthy balances coming into this fiscal year, so these revenue numbers do not pose an immediate crisis. Entering the 2022-23 fiscal year, the SAF had a fund balance of more than \$4.6 billion, and will end this year with some \$3.9 billion. Of that final number, \$1.4 billion is in ongoing funds, while

the remaining \$2.5 billion are one-time COVID-related funds still being expended. The GF/GP will end the year with \$2.6 billion, \$2.3 billion of which is ongoing. However, these latest revenue numbers emphasize the need for careful planning as the legislature completes work on the forthcoming budget to avoid creating a funding cliff as the state comes off the superheated post-COVID revenues.

Another factor to consider when looking at next year's budget is the number of pupils among whom the pot of money will be divided, and each CREC is tasked with establishing this number as well. Current trends appear to show that any students lost during COVID-19 who might be returning to public schools have probably done so. For the current year, the student count is down by 6,200 students and this type of drop is projected to continue for at least the next two years (down 5,600 students in both 2023-24 and 2024-25). As referenced earlier, student numbers are expected to continue dropping as the state population ages, but keep in mind that lower pupil numbers mean more dollars available for distribution when calculated on a per pupil basis.

So, this was a CREC with both good and bad, and as always, there is uncertainty that lies ahead. Governor Whitmer's staff and the legislature will now resolve their three separate budget proposals into a final single budget over the next few weeks. It is expected that we will begin to see the outline of this final agreement in the relatively near future, with the final budget being in place before the end of June. We will update you further as more news becomes available.

Best wishes as you conclude the 2022-23 school year and as you prepare your budget for next year. If you have questions on any of the above, please do not hesitate to contact us!



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