SCHOOL EQUITY CAUCUS

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CAUCUS INFORMATION ALERT

May 17, 2024

Re: Consensus Revenue Estimating Conference

<u>School Aid Fund Revenue Adjusted Downward, Moderate Growth Seen Ahead</u>

Colleagues and Friends:

This morning representatives from the Michigan House and Senate Fiscal Agencies, as well as from the Department of the Treasury (representing the Governor's office), met to arrive at "official" revenue estimates for the current and upcoming fiscal years as part of their semi-annual Consensus Revenue Estimating Conference (CREC). Today'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 the meeting, the parties also hear updates on various elements of the economy to help inform their view of where state revenues may be headed. Economists from the University of Michigan shared projections that the national economy will continue to move forward in the near term, but that momentum is slowing. The inflation rate jumped up in early 2024, causing some delays in expected Federal interest rate cuts. The total inflation rate is currently back over 4%, but when housing is excluded, the rate has been hanging at around 3.5% for some months. The hope is that inflation will continue to moderate over the next three years, but the economists presenting today do not see rates getting down to where they were prior to the pandemic any time in the foreseeable future. Labor markets and most other economic indicators are continuing to revert back to normal, pre-pandemic patterns.

There was also a presentation by an economist from the Federal Reserve Bank of Chicago on the progress of electric vehicle market share within the auto industry, and its potential impact on the Michigan economy. The profitability of electric vehicles remains a major issue. For example, Ford reported a loss of $28,000 per electric vehicle sold last year – a number that is thought to be representative of challenges across the industry as a whole. Moving forward, as electrification continues to progress, there will be a larger and larger impact on revenues that will need to be considered based on the lower collection of taxes connected to gasoline.

Another report that is a part of each CREC is a look at the number of students in public schools across the state. These numbers are important because the number of students compared to the dollars available to spend provide the per pupil amounts that are available for those creating the budget. Today's report found that traditional districts lost 9,155 students this fall (October 2023) while charters increased by 1,126 students (a combined overall decrease of 0.52%). The total number of students in Michigan public schools for the current 2023-24 school year stands at 1,391,200. Looking forward, the total student count anticipated for next year (traditional K-12 plus charters) is being projected at 1.385 million (a decrease of 0.44%), with the following year currently being estimated at an additional drop of 0.47%.

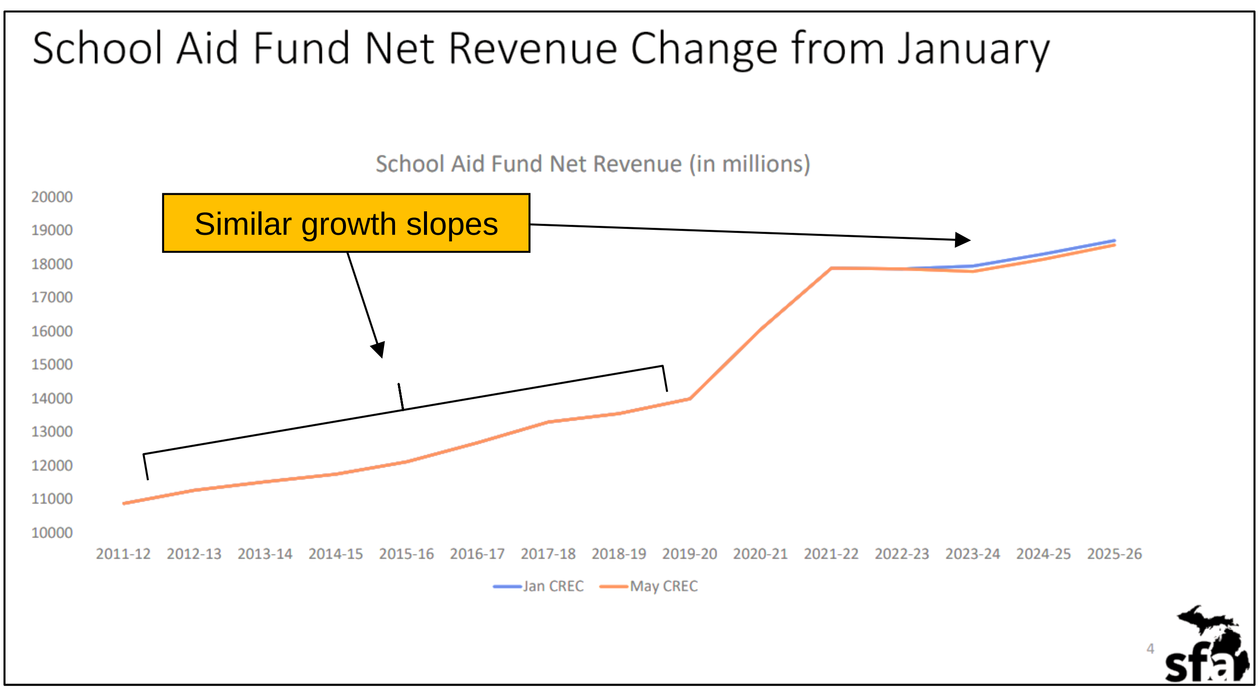
Turning attention to the Michigan revenue picture, income tax growth (both personal and corporate) is being viewed relatively optimistically as things move forward. In particular, corporate income tax revenues have been performing better than expected. In contrast, sales and use taxes as well as business taxes are being projected to grow slowly if at all (depending on the specific tax). In this regard, lower sales tax revenue has a relatively larger impact on the School Aid Fund (SAF), a situation that adversely impacted SAF revenues.

With that as background, here are the numbers…

For the current year (2023-24), SAF growth was originally being projected in January to grow by 0.5%, but is now being projected to actually be <u>down</u> by 0.4% as compared to last year. In real dollar terms, that decrease is represents more than $163 million less revenue than last year.

For next year (2024-25), the percent growth in the SAF is now predicted to be 2.0%, although because the current year's actual dollar figure is lower, next year's actual revenue is also being projected to be lower than previously expected by some $160 million. However, it will still result in revenue of more than $18.1 billion. Looking out even further to the 2025-26 fiscal year, SAF revenues are now being projected to grow during that year by another 2.3%.

The chart below from the Senate Fiscal Agency provides a historical look at the relative growth rate of the SAF over the last several years and looking forward. One can readily see that after the enormous growth of pandemic-era revenues, we have been essentially flat for the last two years. Starting with next year it is expected that we will return to the sort of slow growth seen during the years before COVID.



On the General Fund (GF/GP) side, revenues were moved upward for each of the next three years compared to what was predicted in January. For the current year – which had been projected to see a revenue decrease of 2.6% back in January – projections are now seeing only a relatively small loss of 0.1% ($18 million). While this is not great, it is more than $350 million better than the original decrease projected back in January!

For 2024-25, the GF/GP is being projected to increase by 2.2% (an increase of $309 million over the previous year). With various corporate tax earmarks expiring in 2025-26, that year is expected to see GF/GP revenues increase by a relatively robust 4.4% (an increase of $628.7 million).

Taken together, combined SAF and GF/GP revenues for this year are expected to decrease by just under $95 million (-0.3%) with growth returning over the next two years.

So, what do these numbers mean for the state's balance sheet and for the budget process?

First, the SAF was previously anticipated to close the current year with a balance of some $525 million, but with today's news that number has been lowered to a range between $378 and $426 million (depending on a variety of factors and estimates). This means that there is less money being carried forward to work with for next year, and therefore the various budget proposals put forward must be revised somehow in order to end up with a balance when all is said and done. While the disparities between the House, Senate, and Governor's budgets were already significant, today's reality adds an additional element to the upcoming conference committee negotiations.

Second, moving forward into 2025-26 and beyond, it is even more important for districts to understand that the SAF budget will need to be brought into a more structural balance position. For the last few years, spending has greatly exceeded revenue, but with the projected modest growth in revenue expected over the next few years, this spending pattern will certainly need to change. There has been some insurance built in with the numerous "set-aside" funds where money has been deposited over the past couple of years. However, this additional funding could also quickly evaporate without careful stewardship.

As you hopefully heard this week, a broad coalition of education groups including the MEA, AFT, and education management organizations have urged legislators to reduce the cap on MPSERS UAAL contributions to 13.96% (from the current 20.96%) to reflect the full funding/overfunding of the OPEB (benefit) side of MPSERS. Along with ending the 3% employee contribution that has been mandated for the past several years, this recognition of our successful "full funding" of retirement benefit obligations would mean that the districts, staff, and students who have had to do with less for many years could now utilize these dollars in the classroom. This would also leave the entire pension funding structure intact and on its current trajectory, while providing relief for all those who have sacrificed to bring the benefits side into solvency.

Finally, over the next few years the GF/GP is projected to be in a much healthier growth mode than the SAF. Therefore, it is even more pressing that expenditures related to universities and community colleges must be returned to the GF/GP freeing up SAF for its original intent – the support of K-12 education.

While all of this is being sorted out and until a final budget is negotiated, districts would be wise to take a cautious and conservative approach to their own budgeting. Throughout the process ahead, we will keep you informed as developments warrant, and will continue to advocate for increased funding and the rest of the School Equity Caucus agenda.

As always, your support and advocacy efforts with your legislators is greatly appreciated. If you have any questions, please do not hesitate to contact me. And as the end of another school year approaches, here's hoping you have a very successful wrap-up!

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