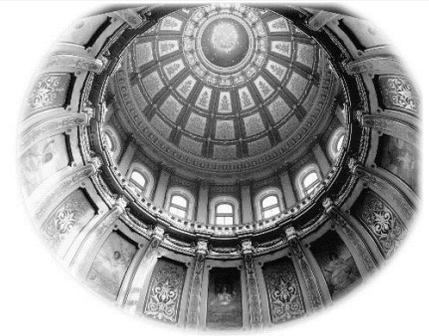


CAPITOL NEWS UPDATE

FY 16-17 BUDGET UPDATE

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McALVEY MERCHANT & ASSOCIATES BUDGET UPDATE NEWSLETTER February 10, 2016

Today, amid loud protests outside the committee room, Governor Snyder presented his FY 16-17 Executive Budget Recommendation. He highlighted four areas in particular: Flint water, Detroit Public Schools, infrastructure, and specialty drugs. Many other areas saw smaller increases and, overall, little new revenue was proposed.

Budget Highlights

Flint response items include: efforts to ensure safe drinking water; food and nutrition interventions; physical, social, and educational well-being programs; water bill relief; and reserve funds designed to be spent over the next two budget cycles.

Funding for Detroit Public Schools (DPS) is proposed to come from securitized tobacco funds, which drew a collective sigh of relief from School Aid Fund and general fund recipients who have been eyeing the \$720 million price tag warily. The total DPS funding would include \$515 million in legacy costs and \$200 million in startup investment for a new system, with a tiny amount remaining on the balance sheet.

To put weight behind the Commission on 21st Century Infrastructure that was announced during the State of the State, the Governor proposes a \$165 million fund. The fund would be used to address prioritized high-risk lead and copper service lines, upgrades while repairing roads or other utilities, and development of asset management plans.

Specialty drug costs are expected to skyrocket to \$131 million to cure Hepatitis-C and improve quality of life for those living with Cystic Fibrosis. To address future costs, the Governor proposes creating a \$30 million reserve fund and including specialty drugs in the State's economic forecast requirements. (These drugs are expected to have a larger impact on the state's budget than even the recent MEGA credit crunch.)

Education

The Administration proposed increases in education, with K-12 schools and higher education coming out ahead of community colleges. K-12 schools see an increase of \$150 million in the foundation allowance using the 2x formula. Individual districts will see increases ranging from \$60 million to \$120 million.

Additionally, the funding formula adjusts to a 50/50 to help address declining enrollment districts. Also included was \$9.0 million for water quality testing in schools. Higher education is proposed to receive an increase that will restore funding to the pre-2011 19% reduction. The increase is 4.3% on average, with tuition restraint recommended at 4.8%, twice the inflation rate.

Capital outlay projects are included for a combined total of seven universities, colleges, and community colleges. Community college operations are proposed to see a smaller 2.4% increase to keep pace with inflation.

Other Areas

In what is believed to be an attempt to avoid election year problems, the Governor also proposed to essentially maintain the status quo in numerous other areas of the budget. Statutory revenue sharing, for example, is proposed to see neither an increase, nor decrease from the current year \$243 million funding level. However, locals will receive a portion of new local transportation funding for roads. The state's new transportation funding system creates a new pool of \$283 million for local roads.

Revenue Increases

There are few fee or revenue increases proposed in the budget, however, there are three items that would increase state revenue. Teacher certification fees are proposed to increase, as have been discussed in the past. The State's Health Insurance Claims Assessment (HICA) is still being targeted for an increase by the administration, just as it has been every year since its creation when it fell short of anticipated revenue. The third area/industry targeted to increase state revenue is auto insurers. The Governor proposed to eliminate a credit recently made available to insurers for deposits into the Michigan Automobile Insurance Placement Facility.

Overall

In general, the Governor's budget targets the state's developing infrastructure and Detroit Public school crises, calls for little new revenue, and attempts to avoid any unnecessary fights with legislators. Many constituencies are satisfied, if not happy, based on initial review of the proposal. Legislators and the fiscal agencies will continue to dive into the details with hearings beginning as early next Tuesday.