From The Capitol

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"May you live in interesting times"
(Ancient Chinese curse)

Interesting times, indeed. Michigan lawmakers are about to embark on deliberations focused on fixing the state's **structural budget deficit**. There will be some winners and some losers, at least in the short term. Both sides will be armed with lobbyist advocates attempting to make their case for saving a program, gaining a carve-out, or protecting any advantage.

Those interests that allow this process to proceed without representation of their interests do so **at their own risk**.

And so, on February 17, Governor Rick Snyder unveiled his first **Executive Budget** and an **overhaul** of Michigan's **business** and **individual tax structure**. Since the Governor's FY 2011-2012 budget is predicated on his tax plan, a look at the Administration's tax proposal both pro and con is in order.

The Synder Plan: Simple, Fair and Efficient
The Pro's and Con's

Business: The Governor's tax plan eliminates the **Michigan Business Tax (MBT)** as we know it, significantly **cutting** business taxes while raising revenues through the personal income tax. Nearly all **credits** for both businesses and individuals would be **eliminated**.

The Snyder proposal calls for the elimination of the MBT with its assessment on both income and gross receipts on all entities. It would be replaced with a **flat 6%** income tax on **"C" corporations only**. Limited liability companies, partnerships and sole proprietorships would not pay any tax because the income of those entities flows to and is recognized by the individual on his/her tax return. This part of the proposal eliminated the **"double taxation"** the latter three entities have undergone since enactment of the MBT in 2007. In addition, the Snyder plan axes the onerous **business surcharge**, literally a tax on the tax businesses owe.

The Snyder proposal also gets rid of all tax credits currently on the books such as those for **brownfield** redevelopment, **historic preservation, renaissance** zones and for **filmmakers**. Nevertheless, the state will honor those business tax credits already given.

Under the Snyder tax proposal it is estimated that by FY 2013 the tax burden on the business community would be **reduced** by over **$1.8 billion**, or nearly two-thirds of what it is today.

Individuals: New sources of state revenue would come from individuals which, it is believed, would more than offset the loss of revenue due to the business tax cuts. The most **controversial** of these new sources will be:

- The imposition of the state income tax on **pensions** for the first time which is expected to raise approximately **$900 million**.
- Elimination of the **Earned Income Tax Credit** for workers with smaller incomes which is expected to raise over **$350 million**.
- A change in Michigan's **Homestead Property Tax Credit**, eliminating the additional credit for those who are 65 years old and older and to lower the income cap on the credit, which is expected to raise approximately **$350 million**.
- Elimination of other **individual tax credits** such as those gained by paying city income tax, donations to public institutions, donations to homeless shelters, food banks, community foundations and historic preservation efforts would raise well over **$150 million**.

In all, the Snyder proposal is the **most sweeping** effort at changes in tax policy in modern history and signifies a dramatic shift toward spreading the tax burden. With its elimination of a whole series of credits for both business and individuals it is both simple and efficient as claimed by the Governor, but **is it fair**? Both sides on the issue are already lining up. Advocates for adversely affected groups are lining up in opposition saying the rich and corporations are being enhanced at the expense of the elderly and poor. Others argue the tax merely spreads the burden evenly and fairly to all in Michigan.

Whether all of the proposals are enacted is still questionable, even with a Legislature dominated by members of the Governor's own political party. Clearly, the imposition of a new **income tax on pensioners** will be the **most politically difficult** facet to sell, especially to the "no new taxes" Republicans. Next on the list is the narrowing of the Homestead Credit.

In the final analysis, the Governor should get much of what he wants from this Legislature. A new **flat tax** on business will probably be **enacted** which will be much simpler than the current MBT. The key on the business tax side is what credits can be saved.

Another Snyder Proposal: A 1% Tax on All Paid Claims To Pay For Medicaid

Believing that the federal government will no longer accept the Quality Assurance Acceptance Program (QAAP) now use tax payments for federal Medicaid matching funds, the Administration proposes a **1% tax** on all paid health care claims. The Governor believes this proposal will be **revenue neutral** with the use tax, raising approximately the same amount ($400 million) as what certain Medicaid providers now pay.

The Governor says enactment of the **tax is essential** in order to keep Medicaid afloat, but the measure could run into serious political trouble. Specifically, there are provider groups that have yet to be taxed and who have successfully resisted the tax, such as physicians. Moreover, insurers with a large market share such as Blue Cross/Blue Shield of Michigan and large employers who are self-insured will object, believing they will be **disproportionately burdened**.

Look for a real dogfight on this issue.

The Budget
Cut and Then Cut Again

The Governor's budget totals nearly **$47 billion** with approximately **$8.1** being General Fund/General Purpose (GF/GP) funding. This represents a 2.5% overall spending decrease from the current fiscal year. The department and programs hardest hit by spending decreases were:

- Statutory revenue sharing – the Governor calls for its elimination
- Higher Education
- Department of Education
- Department of State
- Department of Agriculture
- Department of Civil Rights
- Department of Environmental Quality
- Department of Natural Resources

Earlier last week, the Governor speaking in Detroit before the Business Leaders For Michigan had revealed there would be **no cuts** to Medicaid provider **reimbursement** rates this time around. In fact, the Department of Community Health (DCH) Budget, of which Medicaid is **82%**, received an **11.5%** GF/GP increase under the Snyder proposal. The Governor did emphasize in his presentation that Medicaid funding is dependent upon enactment of an across the board **1%** tax on paid health claims. (Please see previous discussion on the issue)

Local officials are still reeling from the Governor's proposal to **eliminate** statutory **revenue sharing** and replacing it with a **"best practices fund**." Under the proposal, the $200 million used for cities to help defray the cost of services would be granted to cities that employed the use of benchmarks, or best practices, for delivery of services and/or sharing of services.

The Governor also proposes to use the **K-12 school aid fund**, which is expected to have a small surplus, to help fund community colleges. The School Aid Fund is largely state funded so it took a significant hit in an effort to balance the GF/GP Budget. In all, the Snyder budget calls for a **$300 per pupil** cut to schools.

Higher Education also takes a big **18.5% cut** in the Snyder Budget, but the Governor promises no more cuts in future years. Michigan's colleges and universities have taken a big budget hit in recent years and this budget is another **tough pill to swallow**.

The Governor expects to cut the Department of **Corrections** by over **$50 million**. Over a third of these savings would be due to the closing of one prison which has yet to be determined.

Under the Snyder proposal, the Department of **Human Services** would cut **300 workers** and impose a **48 month limit** for the Family Independence cash assistance program.

The Governor proposes to **privatize** some activities conducted by Department of **Agriculture** personnel, such as certain food inspections.

The Administration wants to make the Department of **Environmental Quality** (DEQ) more self-sustaining by increasing **fees**.

In an effort to gain savings, the Governor would eliminate the **Workers' Compensation** Appellate Commission. Cases on appeal would go directly from the board of Magistrates to the Michigan Court of Appeals.

The Governor's Budget calls for **$50 million** of the $550 million that Canada has pledged for the **Detroit River International Crossing** to go toward the state's match for federal transportation funds.

Finally, the Governor proposed **just two omnibus budget bills**, one for general government and one for schools instead of the nearly 20 budget bills that have traditionally been used according to Department or function. By "rolling up" budgets, the Governor contends more value and efficiencies will be gained. While the idea has received a warm reception from House Speaker Jase Bolger, the Senate has yet to get on the bandwagon. A fewer number of bills would also diminish the legislature's role in spending through the use of **boilerplate** language mandates.

Chances of both a tax and budget plan being approved by the May 31 deadline are **50-50** at best but, make no mistake, **significant change** is coming.

Legislation

- Legislation has been introduced (HB 4090) which would create a **Medicaid Inspector General** with a series of very broad powers to police the system.
- Certain members of the Legislature would prohibit a **Third Party Administrator** from entering into a service contract for a benefit plan if the copayment for the service is greater than **50%** of the cost of the service. HB 4057 is thought to enhance reimbursement for some services such as **chiropractic**.
- Another legislative effort has begun to try to reign in **public employee healthcare costs** through "pooling" of benefits and greater contribution levels by public employees. HB 4140 is very similar to last year's plan offered by then Speaker **Andy Dillon**.
- At the Governor's tax and budget presentation, Sen. Bruce Caswell (R-Hillsdale) specifically asked the Budget Director to take a look at the state contract with the current **pharmacy benefit manager** because he (Caswell) believed there were savings that could be achieved.

- The Legislature is about to stifle the Department of **Energy, Labor and Economic Growth** in its efforts to promulgate rules on **ergonomics**. Look for the passage of SB 20 very soon.
- The House will soon pass HB 4214 and accompanying bills which greatly increase the authority of an **emergency financial manager**. The State Treasurer has taken a lead role in development of this legislation due to the foreseen financial crises facing many local governments.
- Look for efforts to improve the **agricultural processing** industry through the use of money from the Michigan 21st Century Jobs Fund.
- Look for major opposition to the Governor's new tax plan from the **Michigan Manufacturers Association** and some major manufacturers in this state.
- Work on the formation of a **Healthcare Exchange** continues in spite of the possibility of the U.S. Supreme court overturning part or all of the federal Affordable Care Act.
- There has been a reintroduction of legislation mandating **insurance coverage** for **autism**. SBs 38 and 39 were introduced last month.
- Look for dentists to introduce legislation **deregulating dental CT scanners**.
- Advanced practice nurses will attempt to increase their scope of practice to include **independent prescriptive authority** and the use and interpretation of diagnostic tests.
- Legislation dealing with specific relief from the gross receipts portion of the Michigan Business Tax (MBT) for the **logistics industry** will be put on the back burner so the full blown effort to repeal the entire tax can begin.
- The battle for a **second crossing** over the **Detroit River** will continue to be waged, with the current bridge owners trying to make a renewed case among the more conservative GOP lawmakers, even though Republican Governor Snyder supports the partnership with the Canadian Government.
- It appears **"financial institutions"** as that term is defined in the MBT are in general agreement to try to keep their 1**.25% premium tax** under the new Snyder plan.