



CAPITOL REPORT

January 12, 2007

The Michigan Legislature began its 2007-08 session Wednesday noon on the same day that **Governor Granholm** announced her creation of a 12 member “emergency financial advisory” panel to make recommendations on the state’s projected \$800 million a year deficit for the current fiscal year and replacement of the \$1.9 billion Single Business Tax which terminates at the end of this calendar year.

Fiscal woes are expected to thoroughly dominate at least the first six months of the legislative term, giving the Republican-controlled Senate (21-17) and Democratic-controlled House (58-52) time for little else. House Dems are expected, however, to try quick passage of legislation ending or altering protection drug companies currently have from Michigan patient suits and legislation regarding trash importation, two of their major campaign issues. Fate of these measures is uncertain in the Senate.

The new advisory panel will be chaired by former Governors **William Milliken** and **James Blanchard**; both of whom won support for income tax increases to wipe out big state deficits during their terms. Among the panel’s other ten members appointed by the Governor are this firm’s **Frank J. Kelley**. Consequently, Mr. Kelley has not participated in the preparation of our comments prepared for this Capitol Report on the State’s tax situation and likely solutions. The views expressed herein are the consensus of all firm members except Mr. Kelley.

Other members of the panel are:

- **Dr. John Porter** - former president of Eastern Michigan University and former state superintendent for public instruction
- **Paul Hillegonds** - senior vice president of DTE Energy and former co-speaker of the House of Representatives
- **Dan DeGrow** - superintendent of St. Clair County Regional Educational Service Agency and former Republican Senate Majority Leader
- **Sr. Monica Kostielney** - president & CEO of the Michigan Catholic Conference
- **Dr. Lou Anna Simon** - president of Michigan State University
- **S. Martin Taylor** - University of Michigan regent

- **John "Joe" Schwarz, M.D.** - former U.S. Congressman and former chair of the state Senate Appropriations Committee
- **Doug Roberts** - former state treasurer under John Engler

Gov. Granholm has given the group until the end of the month to report back on their review of the state's financial crisis and propose solutions to prevent similar crises in the future. That deadline is just ahead of the Governor's State of the State message now scheduled for February 6 and her budget message slated for February 8.

The SBT replacement debate has thus far centered on whether a replacement should be revenue neutral or provide some measure of business tax relief. Also at issue is the exact form of the replacement. The Governor's latest proposal made in early December gained greater support than her earlier proposals, but even the new version has apparently undergone revision by the Governor. When the chips are down, it's hard to see any net tax cut for business coming out of an SBT replacement package.

The existing shortfall, pegged just yesterday at \$800 million, is quite separate from the SBT issue. Skeptics of the advisory panel's creation claim the move is the first step to the Governor proposing new taxes to eliminate or reduce the yawning revenue gap. Whether part of that solution or part of the SBT replacement puzzle, here are the most talked about potential revenue enhancers:

- one cent increase in the sales and use tax (needs public vote to amend the Constitution and raises \$1.4 billion).
- sales tax on some or all services, perhaps in conjunction with one cent reduction in sales tax (raises anywhere from \$1 billion to \$8 billion, depending on breadth of services and amount of tax).
- increase in personal income tax (now 3.9% and would raise \$170 million for each one-tenth of a percent increase).
- graduated income tax (gets rid of flat-rate tax, but needs voter approved Constitutional amendment, which is sure to meet strong opposition).
- package of nuisance taxes (chips away at money shortfall but sure to generate many opposition constituencies).

In terms of **school aid** for the current year, a per pupil executive order cut of up to \$218 per pupil is possible, **BUT** we believe legislators and the Governor will "move heaven and earth" to avoid any cut. At most, we see a \$70 cut and think no cut is a distinct possibility despite all the dire economic news.

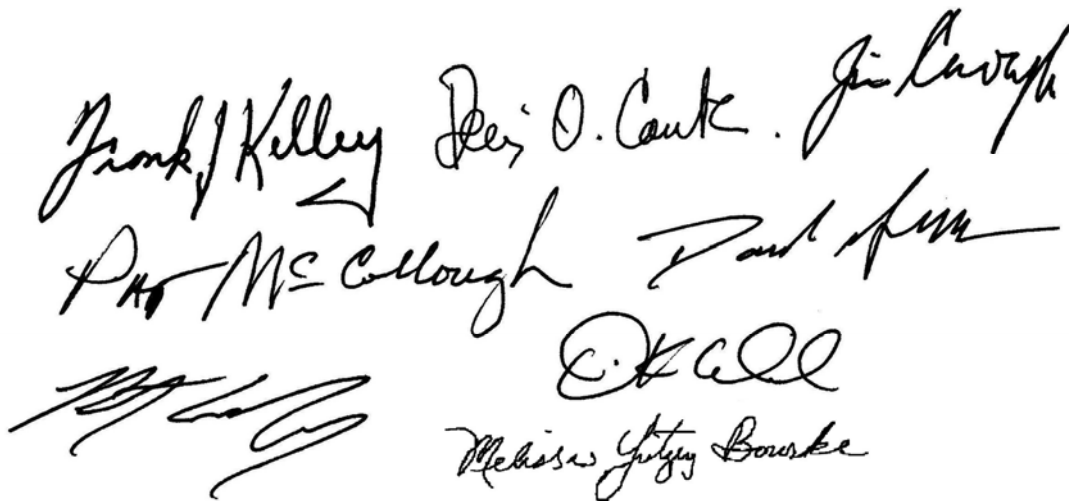
Finally, how do we see the "**fiscal emergency**" playing out? First, the public must be much more sensitized to a crisis situation if a tax hike has any chance of passage. Appointment of the advisory committee is one step in the process. A cut-to-the-bone budget proposal by the Governor is another step, and we expect to see that. Only after dozens of interest groups are

galvanized to save existing state programs will the groundwork be adequately laid for a tax hike. Even then Republican conservatives in the Legislature will be reluctant or unwilling to vote “yes” and majority Democrats in the House will be terrified that a “yes” vote by their most vulnerable new members will lead to recalls of the kind that in early 1984 dumped Senate Dems from a majority which they have failed to regain ever in the intervening 23 years.

In the end, we wouldn't be surprised to see the Legislature place one, or competing, revenue proposals on the ballot for the voters to decide, much like what was done in 1993 to settle the old, seemingly intractable property tax/school finance deadlock. Even going this route will not involve easy choices for politically nervous legislators but it may be the only option left at the end of the day. 2007 will indeed be an exciting year at the State Capitol!

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Notes: **Mary Lannoye**, former state budget director, is Gov. Granholm's new Chief of Staff...Former Senate Dem leader **Bob Emerson** is her successor at DMB...New House Speaker **Andy Dillon** (D-Redford) said in session opening remarks that “partisanship ran amok” in the last legislature. He said his chamber will move quickly, including session on Mondays, to expand access to affordable health care, strengthen the education system, fix the state's structural deficit, tackle Michigan's energy needs and make the state a magnet for 21st Century Jobs by implementing a tax structure that rewards investment...New Senate Majority Leader **Mike Bishop** (R-Rochester) said consolidation of local governments should be looked at, and new Senate Appropriations chair **Ron Jelinek** (R-Three Oaks) left the door open to his supporting a sales tax on services coupled with a reduction of the sales tax...**Kathleen Straus** has again been elected president of the State Board of Education.



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2007 – 2008 MICHIGAN LEGISLATURE

SENATE

Majority Leader:
Mike Bishop (R-Rochester)

Majority Floor Leader:
Alan Cropsey (R-DeWitt)

President Pro Tem:
Alan Sanborn (R-Richmond)

Appropriations Chair:
Ron Jelinek (R-Three Oaks)

Minority Leader:
Mark Schauer (D-Battle Creek)

Minority Floor Leader:
Buzz Thomas (D-Detroit)

Ranking Appropriations Member:
Mike Prusi (D-Ispeming)

HOUSE

Speaker:
Andy Dillon (D-Redford)

Speaker Pro Tem:
Michael Sak (D-Grand Rapids)

Majority Floor Leader:
Steve Tobocman (D-Detroit)

Appropriations Chair:
Probably George Cushingberry (D-Detroit)
or Alma Wheeler Smith (D-Ann Arbor)

Minority Leader:
Craig DeRoche (R-Novi)

Minority Floor Leader:
Chris Ward (R-Brighton)

Ranking Appropriations Member:
Member – not yet appointed