



STATE OF MICHIGAN
STATE BUDGET OFFICE
LANSING

RICK SNYDER
GOVERNOR

JOHN E. NIXON, CPA
DIRECTOR

June 27, 2011

Michigan State Senate
c/o Ms. Carol Morey Viventi, Secretary
State Capitol
Lansing, Michigan 48909

Michigan House of Representatives
c/o Mr. Gary L. Randall, Clerk
State Capitol
Lansing, Michigan 48909

Dear Ms. Morey Viventi and Mr. Randall:

Transmitted under this cover is a schedule entitled "Statement of Revenue Subject to Constitutional Limitation - Legal Basis." The statement is submitted pursuant to Sections 18.1350(a) through 18.1350(e) of the Michigan Compiled Laws for the purpose of demonstrating compliance with Article 9, Section 26 of the Michigan Constitution for the fiscal year 2010.

The statement has been reviewed by the Office of the Auditor General and a copy of the independent accountant's review is enclosed.

If you have questions regarding this report, please contact Mr. Michael J. Moody, Director, Office of Financial Management, at 373-1010.

Sincerely,

A handwritten signature in black ink, appearing to read "John E. Nixon".

John E. Nixon, C.P.A.
State Budget Director

Enclosure

cc: D. Posthumus, Executive Office
Senate Appropriations Committee
House Appropriations Committee
Ellen Jeffries, Senate Fiscal Agency
Mitchell Bean, House Fiscal Agency



STATE OF MICHIGAN
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

The Honorable Rick Snyder, Governor
Members of the Legislature

We have reviewed the accompanying statement of revenue subject to constitutional limitation (legal basis) of the State of Michigan for the fiscal year ended September 30, 2010 in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. All information included in the accompanying statement is the representation of the State's management.

A review consists principally of inquiries of agency personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

As described in Note 1, the accompanying statement was prepared in accordance with Sections 18.1350a - 18.1350e of the *Michigan Compiled Laws*, which provide statutory language to implement Article IX, Sections 26 and 33 of the Michigan Constitution. Accordingly, the financial statement is not intended to be presented in conformity with accounting principles generally accepted in the United States of America.

Based on our review, we are not aware of any material modifications that should be made to the accompanying statement of revenue subject to constitutional limitation (legal basis) of the State of Michigan for the fiscal year ended September 30, 2010 in order for it to be in conformity with the basis of accounting described in Note 1.

This report is intended solely for the information and use of the Governor, the Legislature, and the State's management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

June 10, 2011

STATE OF MICHIGAN
STATEMENT OF REVENUE SUBJECT TO
CONSTITUTIONAL LIMITATION

(LEGAL BASIS)

FISCAL YEAR ENDED SEPTEMBER 30, 2010

Prepared by

State Budget Office
Office of Financial Management

June 10, 2011

STATE OF MICHIGAN
STATEMENT OF REVENUE SUBJECT TO CONSTITUTIONAL LIMITATION - LEGAL BASIS
 Fiscal Year Ended September 30, 2010
 (In Millions)

Total Revenue and Other Financing Sources - General, Special Revenue and Permanent Funds (Note #2)		\$ 47,369.5
Less Statutory Exclusions (Note #3):		
Interfund transfers between General, special revenue, and permanent funds	\$ 1,372.0	
Interfund borrowing costs	1.1	
Proceeds from bonds and notes	64.6	
Financing provided by capital leases	39.1	
Federal revenue	19,463.9	
Debt service	107.5	
Property tax credits (Note #4)	993.4	
Other statutory exclusions:		
Special Medicaid reimbursements	123.2	
Tobacco settlement reimbursements	198.7	
Prior year expenditure reimbursements	122.1	
Other exclusions	<u>152.4</u>	(22,637.9)
Addition for Refundable and Nonrefundable Tax Credits (Note #4)		<u>841.0</u>
Total Revenue Subject to Limitation		<u>\$ 25,572.6</u>
2008 Personal Income (Note #5)		\$ 349,612.0
Section 26 Base Ratio (Note #6)		<u>x 9.49%</u>
Section 26 Revenue Limitation		33,178.2
Total Actual Revenue Subject to Limitation		<u>25,572.6</u>
Amount Over (Under) Limit		<u>\$ (7,605.6)</u>

The accompanying footnotes are an integral part of this financial statement.
 Column detail may not add to totals because of rounding.
 See Independent Accountant's Review Report.

NOTES TO THE STATEMENT OF REVENUE SUBJECT TO
CONSTITUTIONAL LIMITATION - LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2010

1. Basis of Accounting and Presentation

The Statement of Revenue Subject to Constitutional Limitation - Legal Basis is presented in compliance with Public Act 504 of 1988, primarily Sections 18.1350a - 18.1350e of the Michigan Compiled Laws (MCL). P.A. 504 provides statutory language to implement Article 9, Sections 26 and 33 of the State Constitution. These legal provisions, which prescribe how compliance with the revenue limitation is determined, are outlined in the notes that follow. This statement is not intended to be a presentation in accordance with generally accepted accounting principles.

MCL Section 18.1350a provides that the calculation of State revenue shall not be adjusted after the filing of the report required for June 30, 1989, unless changes in generally accepted accounting principles would substantially distort the comparability of the base year. Because of changes in those principles and to provide comparability to the base year report, State revenues in this report include the General Fund, select special revenue funds, and permanent funds.

2. Total Revenue and Other Financing Sources

P.A. 504 defines total State revenue, for the purpose of determining the revenue limit, as the combined increase in net current assets of the General and special revenue funds. The amount on the line entitled "Total Revenue and Other Financing Sources – General, Special Revenue, and Permanent Funds" is calculated based on revenues reported in the *State of Michigan Comprehensive Annual Financial Report* (SOMCAFR). These revenues are derived using generally accepted accounting principles (GAAP). Additional information regarding the State's revenue recognition and accrual policies are included in Note #1 (Summary of Significant Accounting Policies) and Note #6 (Taxes Receivable) of the 2010 SOMCAFR.

3. Statutory Exclusions

P.A. 504 provides for exclusions from the revenue limit. These exclusions are provided for two primary reasons: 1) to eliminate those revenue sources which are excluded under Article 9, Section 33 of the State Constitution; and 2) to eliminate duplicate revenue arising from the methods used to account for the recognition of certain financial resources and the flow of these resources between the General Fund, special revenue, and permanent funds. The specific exclusions from the revenue limit are as follows:

- a. Financing sources which have previously been counted as revenue for purposes of the revenue limit, such as beginning fund balance, expenditure refunds including reimbursement of tobacco-related health costs and prior year accounts payable write-offs, and transfers between the funds included in the calculation of revenue subject to Constitutional limitation.

During fiscal year 2010, the General Fund incurred short-term interfund borrowing costs, resulting in interest income to select special revenue and permanent funds totaling \$1.1 million. This interest income has been excluded from the calculation of State revenue, similar to the treatment used for transfers.

- b. Current assets generated from transactions involving capital assets and long-term obligations in which total net assets do not increase, such as capital lease transactions and financing provided by bond proceeds.
- c. Revenues, such as Special Medicaid reimbursements and child support collections, which are not available for normal public functions of the General Fund, special revenue, and permanent funds.

NOTES TO THE STATEMENT OF REVENUE SUBJECT TO
CONSTITUTIONAL LIMITATION - LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2010 (CONTINUED)

- d. Federal aid is excluded in the line entitled "Federal revenue."
 - e. Taxes imposed for the payment of principal and interest on voter approved bonds and loans to school districts authorized under Article 9, Section 16 of the State Constitution. This revenue is excluded in the line entitled "Debt service."
 - f. Tax credits based on actual tax liabilities including the imputed tax components of rental payments (See Note #4).
 - g. Refunds or payments of revenues recognized in a prior period include out of period tax refunds.
 - h. The effects of restatements of beginning fund balances required by changes in generally accepted accounting principles.
4. Tax Credits

General: The Constitution requires that "...Total State Revenues shall exclude the amount of any credits based on actual tax liabilities or the imputed tax components of rental payments, but shall include the amount of any credits not related to actual tax liabilities...." This language results in adjustments to the revenue reported in the GAAP-based SOMCAFR "Schedule of Revenue and Other Financing Sources" to compute the amount of revenue subject to the revenue limit.

The State's tax laws provide for several types of individual income and Michigan business tax credits. Some credits are accounted for as revenue reductions in the SOMCAFR while others are reported as revenues and expenditures. The accounting and type of credit determines the adjustment to revenue that is necessary, as described below.

Statutory exclusion for property tax credits: Revenues and expenditures are reported in SOMCAFR for individual income tax credits which can be received even if they exceed the individual's tax liability (i.e., "refundable" tax credits). The property tax credit is the primary credit that falls into this category. All refundable individual income tax credits must be included in revenue for purposes of computing total State revenue subject to limitation, except for the property tax credit. Because these credits are reported as revenues and expenditures, the property tax credits for the year are subtracted from total State revenue subject to limitation on the line "Property tax credits" on the Statement of Revenue Subject to Constitutional Limitation - Legal Basis.

Addition for certain refundable and nonrefundable tax credits: Revenue reductions are recorded for those individual income tax credits that are limited by the amount of an individual's tax liability before considering such credits (i.e., "nonrefundable" tax credits). Revenue reductions are also recorded for both refundable and nonrefundable Michigan business tax credits. Those credits that do not meet the statutory exclusion described in Note #3 must be added back to the total State revenue subject to limitation. This adjustment totaled \$66.7 million in individual income tax credits and \$774.3 million in Michigan business tax credits and is reported on the line "Addition for Refundable and Nonrefundable Tax Credits" on the Statement of Revenue Subject to Constitutional Limitation - Legal Basis.

The adjustment for Michigan business tax credits is significantly larger than in prior years because it was determined that prior year calculations did not include all applicable business tax credits. However, the addition of these credits in prior years would not result in actual revenue exceeding the revenue limitation.

NOTES TO THE STATEMENT OF REVENUE SUBJECT TO
CONSTITUTIONAL LIMITATION - LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2010 (CONTINUED)

5. Personal Income of Michigan

Personal income of Michigan is defined by Article 9, Section 33 of the State Constitution as total income received by persons in Michigan from all sources, as defined and officially reported by the United States Department of Commerce (USDOC), or its successor agencies. Article 9, Section 26 of the State Constitution requires that the personal income of Michigan for 1977 be used for computing the fiscal year 1979 limit. For each subsequent year's computation, personal income of Michigan for a calendar year is defined by MCL Section 18.1350a(a) as total annual personal income as officially reported by USDOC.

6. Section 26 Base Ratio

The Section 26 base year ratio is 9.49%. This is the ratio of fiscal year 1979 "Total Revenue Subject to Limitation," to the calendar year personal income of Michigan in 1977 (See Note #5).