RICK SNYDER
GOVERNOR

STATE OF MICHIGAN
STATE BUDGET OFFICE
LANSING

JOHN S. ROBERTS
DIRECTOR

June 13, 2016

Michigan State Senate
c/o Mr. Jeff Cobb, Secretary
State Capitol
Lansing, MI 48909

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

Dear Mr. Cobb and Mr. Randall:

This letter transmits the "Statement of the Proportion of Total State Spending From State Sources Paid to Units of Local Government - Legal Basis" for fiscal year 2015, which has been prepared in accordance with Sections 18.1115(5), 18.1303-18.1305, 18.1349, 18.1350, 18.1497, and 18.1498 of the Michigan Compiled Laws for the purpose of demonstrating compliance with Article 9, Section 30 of the Michigan Constitution.

The computed percentage of total state spending from state sources paid to local governments for fiscal year 2015 is 55.25%, which is $1.9 billion more than the minimum required.

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

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

Sincerely,

John S. Roberts
State Budget Director

Enclosure

cc: D. Posthumus, Executive Office
Senate Appropriations Committee
House Appropriations Committee
Ellen Jeffries, Senate Fiscal Agency
Mary Ann Cleary, House Fiscal Agency

OAG
Office of the Auditor General
Doug A. Ringler, CPA, CIA
Auditor General
201 N. Washington Square, Sixth Floor • Lansing, Michigan 48913 • Phone: (517) 334-8050 • www.audgen.michigan.gov

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

The Honorable Rick Snyder, Governor
Members of the Legislature

We have reviewed the accompanying Statement of the Proportion of Total State Spending From State Sources Paid to Units of Local Government - Legal Basis (Statement) of the State of Michigan for the fiscal year ended September 30, 2015. A review includes primarily applying analytical procedures to management's financial data and making inquiries of management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the accompanying statement as a whole. Accordingly, we do not express such an opinion.

Management is responsible for the preparation and fair presentation of the accompanying Statement in accordance with Sections 18.1115(5), 18.1303 - 18.1305, 18.1349, 18.1350, 18.1497, and 18.1498 of the *Michigan Compiled Laws*, which provide statutory language to implement Article IX, Section 30 of the Michigan Constitution, and for designing, implementing, and maintaining internal control relevant to the preparation and fair presentation of the accompanying Statement.

Our responsibility is to conduct the review in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the accompanying Statement. We believe that the results of our procedures provide a reasonable basis for our report.

The accompanying Statement was prepared for the purpose of complying with the *Michigan Compiled Laws* cited above, as discussed in Note 1, and is not intended to be a presentation 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 for the fiscal year ended September 30, 2015 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.

Sincerely,

Doug Ringler

Doug Ringler
Auditor General
June 7, 2016

State of Michigan

Statement of the Proportion of Total State Spending From State Sources Paid to Units of Local Government Legal Basis

Fiscal Year Ended September 30, 2015

Prepared by

State Budget Office
Office of Financial Management

June 7, 2016

MICHIGAN
STATEMENT OF THE PROPORTION OF TOTAL STATE SPENDING FROM STATE SOURCES
PAID TO UNITS OF LOCAL GOVERNMENT-LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2015
(In Millions)

TOTAL STATE SPENDING (Note 2)		
Expenditures and Transfers		
General Fund	$ 33,353.2	
Other Operating Funds	18,867.3	
Nonoperating Funds and Component Units	97.2	
Adjustment to General Fund Expenditures and Transfers	(21.5)	
Total Net Expenditures and Transfers:		$ 52,296.3
Interfund Transfer Deductions (Note 2)		
From General Fund to Other Operating Funds	(140.2)	
From Other Operating Funds to General Fund and to Other Operating Funds	(1,060.7)	
Subtotal	(1,200.9)	
Less Interfund Transfer of Federal Funds	1.6	
Total Interfund Transfer Deductions:		(1,199.3)
Expenditure Adjustments (Note 3)		
Debt Service	(274.8)	
Refunds (net)	(365.6)	
Accounts Receivable Write-Off	(12.8)	
Total Expenditure Adjustments:		(653.2)
TOTAL STATE SPENDING		50,443.8
NON-STATE FUNDING		
Federal Revenue	(20,728.9)	
Local Revenue	(147.9)	
Private Revenue (Note 4)	(137.0)	
Total Non-State Funding:		(21,013.9)
Budget Stabilization Fund (Note 5)		
Deposits	94.0	
Withdrawals	-	
Total Budget Stabilization Fund Adjustments:		94.0
TOTAL STATE SPENDING FROM STATE SOURCES		$ 29,523.9
STATE SPENDING PAID TO UNITS OF LOCAL GOVERNMENT		$ 16,313.1
PROPORTION OF TOTAL STATE SPENDING FROM STATE SOURCES PAID TO UNITS OF LOCAL GOVERNMENT (Notes 2 and 6)		55.25%
Excess of actual payments to units of local government over minimum proportion required of 48.97% (Note 6)		$ 1,855.2

The accompanying notes are an intregal part of this financial statement.
Note that column detail may not add to totals because of rounding.
See Independent Accountant's Review Report.

MICHIGAN
NOTES TO THE STATEMENT OF THE PROPORTION OF TOTAL STATE SPENDING FROM STATE SOURCES PAID TO UNITS OF LOCAL GOVERNMENT - LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2015

NOTE 1 – BASIS OF ACCOUNTING AND PRESENTATION

The accompanying Statement of the Proportion of Total State Spending From State Sources Paid to Units of Local Government - Legal Basis is presented in accordance with legal requirements set forth in Sections 18.1115(5), 18.1303 - 18.1305, 18.1349, 18.1350, 18.1497, and 18.1498 of the Michigan Compiled Laws (MCL). These sections provide statutory language to implement Article 9, Section 30 of the State Constitution. This statement is not intended to be a presentation in accordance with generally accepted accounting principles.

NOTE 2 – STATUTORY DEFINITIONS

The following definitions were used in the preparation of the financial statement:

a. Total State Spending – MCL Section 18.1305(1) defines total State spending as the sum of State operating fund expenditures, not including transfers for financing between funds. Transfers between operating funds continue to be excluded from total State spending, which eliminates the potential for duplicate counting. Transfers from operating funds to nonoperating funds are not excluded, however, and are considered a part of total State spending.

b. State Operating Fund – MCL Section 18.1304(2) defines a State operating fund as a State fund entity established by law to provide direct financial support for services delivered to the public pursuant to the State budget. Prior to fiscal year 2001, the State's operating funds consisted of the General Fund and select special revenue funds. The State's implementation of the Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments, for fiscal year 2001 resulted in some operating funds being reclassified as permanent funds. The State's implementation of GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, for fiscal year 2011 resulted in some operating funds being reclassified as capital projects funds. Accordingly, the financial statement includes the General Fund, the permanent funds, and certain special revenue and capital projects funds of the State of Michigan.

   The financial statement also includes nonoperating fund and component unit appropriated administrative expenditures. The expenditures have been included because, during the computation of the base year proportion of total State spending from State sources paid to units of local government, the expenditures were recorded in the General Fund. The inclusion of these expenditures provides for consistency of the current year computation with the base year.

   The financial statement excludes certain General Fund expenditures on the line titled "Adjustment to General Fund Expenditures and Transfers." These expenditures are excluded because, during the computation of the base year, the expenditures were recorded in funds that were not considered operating funds. The exclusion of these expenditures provides for consistency of the current year computation with the base year.

c. Total State Spending From State Sources – MCL Section 18.1305(2) defines total State spending from State sources as the sum of State operating fund expenditures, not including transfers for financing between funds, federal aid, and restricted local and private sources of financing.

d. Unit of Local Government – MCL Section 18.1115(5) defines a unit of local government as a political subdivision of this State, including school districts, community college districts, intermediate school districts, cities, villages, townships, counties, and authorities, if the political subdivision has as its primary purpose the providing of local governmental services for citizens in a geographically limited area of the State and has the power to act primarily on behalf of that area.

e. State Spending Paid to Units of Local Government – MCL Section 18.1304(3) defines State spending paid to units of local government as the sum of total State spending from State sources paid to a unit of local government. The section further provides that State spending paid to units of local government does not include payments made under a contract agreement for the providing of services to the State or to State property, and loans made by the State to a unit of local government.

   Also included in total State spending paid to units of local government are payments made on behalf of units of local government. Section 18.1350 requires the inclusion of expenditures as payments to units of local government if the expenditures relate to functions performed by the units of local government and the State assumed the financing and administration of the function after December 22, 1978.

f. Proportion of State Spending From State Sources Paid to Units of Local Government – MCL Section 18.1303(5) defines it as the proportion of total State spending from State sources paid to all units of local government in a fiscal year. This proportion shall be calculated by dividing a fiscal year's State spending from State sources paid to units of local government by total State spending from State sources for the same fiscal period. The proportions as calculated are expressed in terms of percentages.

NOTE 3 – EXPENDITURE ADJUSTMENTS

Debt Service - Revenue dedicated to the repayment of voter approved bonds and loans to school districts authorized under Article 9, Section 16, of the State Constitution is not considered a State source for purposes of the computation of the State revenue limit under Article 9, Section 26, of the State Constitution. Therefore, expenditures recorded for the actual debt service payments are also not considered to be State spending from State sources for this statement.

Refunds – MCL Section 18.1350(2) states that refunds or other repayments of prior year revenues shall not be considered in the determination of total State spending. As such, the following adjustments have been made to total State spending:

a. As explained in more detail in the *State of Michigan Comprehensive Annual Financial Report*, the State accounts for certain income tax credits as expenditures. These expenditures, the most significant of which are related to property taxes, were not considered expenditures in the base year and are, therefore, subtracted in determining total State spending to provide consistency with the base year.

b. Certain individual income and Michigan business tax credits that are not based on actual tax liabilities are added back to State spending by reducing the "refunds" exclusion for other credits. The reason for counting these tax credits as total State spending is that the tax revenues, which finance the tax credit programs, are considered State sources of financing for the purposes of the computation of total State revenue as defined by Article 9, Section 26 of the State Constitution. Because the tax revenue is considered a State source of revenue, the expenditure of the revenue is considered State spending for purposes of this statement.

c. Tax refunds that are recorded in a fiscal year after the tax revenue has been recognized are recorded as expenditures, rather than as revenue reductions. Therefore, these refunds of prior year revenue have been subtracted in order to exclude them from total State spending.

Accounts Receivable Write-offs - Write-offs of prior year accounts receivable are recorded as expenditures. Because the write-off of a prior year accounts receivable is an adjustment to prior year revenue, the amount of such write-offs recorded as an expenditure is subtracted to be appropriately excluded from total State spending.

NOTE 4 – PRIVATE REVENUE

Private revenue has generally been defined for the preparation of this statement as revenue received from nonpublic entities, in which the use is restricted by the entity remitting the revenue or restricted by the State Constitution, statute, or an appropriation act. A statutory definition has not been developed. The largest components of fiscal year 2015 private revenues are hospital contributions ($78.2 million), child support offset collections ($13.9 million), and collections for care of patients, wards, and inmates ($15.4 million).

The child support offset collections are received by the State Disbursement Unit from State and federal tax return offsets. The amounts collected are reimbursements to the State for excess payments made by the Temporary Assistance to Needy Families program. Also, a portion of the collections must be returned to the federal government as a repayment of the federal share of the excess Temporary Assistance to Needy Families payments. The hospital contributions were voluntary contributions received from hospitals and restricted for use to finance increased payments to hospitals with a disproportionate share of indigent clients. The collections for care of patients, wards, and inmates are from the individuals in State custody, their families, or insurance providers to reimburse the State for a portion of the cost of care provided to these individuals.

NOTE 5 – BUDGET STABILIZATION FUND ADJUSTMENTS

Deposits to the Counter-Cyclical Budget and Economic Stabilization Fund are added to total State spending. When withdrawals are made from the fund, the withdrawal is subtracted from total State spending, so that the funds previously deposited are not counted as spending twice.

During fiscal year 2015, the fund received a deposit of $94.0 million from the General Fund.

During fiscal year 2014, $194.8 million was transferred to the Michigan Settlement Administration Authority to support the Detroit bankruptcy settlement. The withdrawal will be repaid to the fund in the amount of $17.5 million annually from tobacco settlement funds, beginning in fiscal year 2015. Repayments are not included in deposits to avoid double counting as the funds were added to State spending at the time of their original deposit.

NOTE 6 – BASE YEAR SPENDING PROPORTION

Article 9, Section 30 of the State Constitution requires the State to maintain the proportion of State spending to local units in at least the same proportion as that which was in effect in fiscal year 1979 (base year). The base year proportion was originally computed to be 41.61%.

Effective with fiscal year 1993, a recalculation was made of the base year proportion as a consequence of a settlement agreement reached on the County of Oakland v State of Michigan lawsuit, which was settled in 1991. The recalculated base year proportion is 48.97%.