JENNIFER M. GRANHOLM
GOVERNOR

STATE OF MICHIGAN
OFFICE OF THE STATE BUDGET
LANSING

ROBERT L. EMERSON
DIRECTOR

June 29, 2010

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

Michigan House of Representatives
c/o Mr. Richard J. Brown, Clerk
State Capitol
Lansing, MI 48909

Dear Ms. Morey Viventi and Mr. Brown:

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 2009, 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 2009 is 58.53%, which is $2.5 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,

Robert L. Emerson
State Budget Director

Enclosure

cc: T. Hughes, Legislative Affairs
Senate Appropriations Committee
House Appropriations Committee
Gary Olson, Senate Fiscal Agency
Mitchell Bean, House Fiscal Agency

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

The Honorable Jennifer M. Granholm, 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) of the State of Michigan for the fiscal year ended September 30, 2009 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 18.1115(5), 18.1303 - 18.1305, 18.1349, 18.1350, 18.1497, and 18.1498 of the *Michigan Compiled Laws,* which provides statutory language to implement Article IX, Section 30 of the Michigan Constitution. Accordingly, the financial statement 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 of the proportion of total State spending from State sources paid to units of local government (legal basis) of the State of Michigan for the fiscal year ended September 30, 2009 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 17, 2010

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, 2009

Prepared by

State Budget Office
Office of Financial Management

June 17, 2010

STATEMENT OF THE PROPORTION OF TOTAL STATE SPENDING FROM STATE SOURCES PAID TO UNITS OF LOCAL GOVERNMENT-LEGAL BASIS
FISCAL YEAR ENDED SEPTEMBER 30, 2009
(In Millions)

TOTAL STATE SPENDING (Note 2)		
Gross Expenditures and Transfers		
General Fund	$ 27,148.0	
Other Operating Funds	18,140.0	
Nonoperating Funds and Component Units	80.6	
Total Gross Expenditures and Transfers:		$ 45,368.5
Interfund Transfer Deductions (Note 2)		
From General Fund to Other Operating Funds	(85.5)	
From Other Operating Funds to General Fund and to Other Operating Funds	(1,023.4)	
Subtotal	(1,108.9)	
Less: Interfund Transfer of Federal Funds	1.5	
Total Interfund Transfer Deductions:		(1,107.4)
Expenditure Adjustments (Note 3)		
Debt Service	(105.2)	
Refunds	(897.2)	
Accounts Receivable Write-Off	(29.9)	
Total Expenditure Adjustments:		(1,032.3)
TOTAL STATE SPENDING		43,228.9
NON-STATE FUNDING		
Federal Revenue	(17,073.5)	
Local Revenue	(191.6)	
Private Revenue (Note 4)	(129.2)	
Total Non-State Funding:		(17,394.3)
TOTAL STATE SPENDING FROM STATE SOURCES		$ 25,834.6
STATE SPENDING PAID TO UNITS OF LOCAL GOVERNMENT		$ 15,122.2
PROPORTION OF TOTAL STATE SPENDING FROM STATE SOURCES PAID TO UNITS OF LOCAL GOVERNMENT (Notes 2 and 5)		58.53%
Excess of actual payments to units of local government over minimum proportion required of 48.97% (Note 5)		$ 2,471.0

The accompanying notes are an intregal part of this financial statement.
See Independent Accountant's Review Report

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, 2009

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.

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 Standard Board 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 re-classified as permanent funds. Accordingly, the financial statement includes the General Fund and certain special revenue and permanent 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.

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.

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 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 credits added back, and therefore included in total State spending, are: the credits on the income, Michigan Business taxes for donations to institutions of higher education; the community foundation credit; college tuition credit; historical preservation credit; and the homeless foodbank credit.

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.

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 2009 private revenues are hospital contributions ($61.1 million), child support offset collections ($36.5 million), and collections for care of patients, wards, and inmates ($20.7 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.

5. 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%.