Senate Fiscal Agency
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BILL ANALYSIS

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House Bill 4657 (as reported without amendment)
Sponsor: Representative Glenn Oxender
House Committee: Tax Policy
Senate Committee: Education

Date Completed: 6-7-95

RATIONALE

Voter approval of Proposal A on March 15, 1994, put in place a new school financing system for the State. As part of this new finance plan, various tax revenues are statutorily or constitutionally dedicated to the School Aid Fund, but not all of the money needed to fund schools comes from these dedicated sources. Consequently, the Legislature annually must make an appropriation from the General Fund to the School Aid Fund. In formulating the school finance reform offered in Proposal A, a goal for some people apparently was to guarantee State funding for public elementary and secondary schools. It has been proposed that additional income tax revenues be dedicated to the School Aid Fund so that General Fund support would not be needed.

CONTENT

The bill would amend the Income Tax Act to increase from 14.4% to 29% the amount of gross collections before refunds from the income tax that is deposited in the State School Aid Fund. The increase would take effect after September 30, 1996.

MCL 206. 51

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The State School Aid Fund currently is made up of earmarked revenues, a grant from the General Fund, one-time revenue items, and a carry-over surplus. Although a large portion of the funding for schools is made up of dedicated revenues, the School Aid Fund still depends on a substantial contribution from the General Fund. By increasing from 14.4% to 29% the amount of income tax revenues dedicated to the School Aid Fund, the bill would lock in additional State tax revenues for school funding. This would take schools out of the competition for General Fund revenues and would provide additional protection for school funding.

Response: The bill would guarantee that schools received a higher percentage of State income tax revenues, but would not ensure that actual funding amounts would be maintained. If the State's economy were to experience a recession, for example, the amount of income tax revenues could decrease. In this case, the School Aid Fund still would receive 29% of the revenues, but the total amount of funds would be smaller. Thus, the contribution to the School Aid Fund would be less. Conversely, as the economy improved, tax revenues would increase and the actual amount of funds for schools would increase. The bill would protect a certain portion of tax revenues for schools, but schools still would be affected by changes in the State's economy.

Supporting Argument

With the implementation of the State's new school financing system, most of the new tax collections began May 1, 1994, even though the revenues were not needed until the State's 1995 fiscal year. As a result, the School Aid Fund had a surplus at the end of the 1994 and 1995 fiscal years. It is estimated that the surplus resulting from the early tax collection will be exhausted by the 1997 fiscal year. The bill would increase to 29% the percentage of State income tax revenue dedicated to the School Aid Fund. Using the 1995 and 1996 State fiscal years as a base, it is estimated that the 29% dedication would be sufficient to replace the General Fund contribution as well as the one-time revenue items and the carry-over surplus that are built into the proposed 1996 School Aid budget.

Response: An increase in the percentage of State income tax revenue dedicated to schools would maintain current funding levels for schools in the 1996 fiscal year, but it is not certain that it would generate sufficient funding for schools in subsequent fiscal years. Some people believe that a greater percentage of these revenues should be dedicated to schools to ensure adequate State support in the future.

Opposing Argument

By transferring more tax revenues to the School Aid Fund, the bill would result in a net loss to the General Fund. Consequently, other worthy State programs, such as corrections operations, would have to compete for fewer General Fund dollars. Furthermore, earmarking additional State revenue to the School Aid Fund is unnecessary, since the constitutional provisions under Proposal A already protect school funding in future years. In addition, increasing the percentage of income tax revenue dedicated to school aid would limit the State's flexibility in making budget decisions.

Response: By ensuring that schools did not have to compete with other departmental budgets for State General Fund money, the bill would make it clear that adequate funding for the State's educational system had top priority.

Legislative Analyst: L. Arasim

FISCAL IMPACT

This bill would have a fiscal impact on both the School Aid Fund (SAF) and the General Fund beginning in FY 1996-97. Since revenue and spending estimates for FY 1996-97 have not yet been made, to help illustrate the fiscal impact this bill would have, this analysis uses data for FY 1995-96. Under current law, 14.4% of income tax revenue is earmarked to the SAF; the earmarked revenue is estimated to total $916.2 million in FY 1995-96. Increasing the earmarking to 29% of income tax collections, would allocate an additional $929 million to the SAF, for a total of $1,845.2 million. The additional earmarking of $929 million would be large enough to replace the GF/GP grant to the SAF, plus several one-time revenue items that are being used in FY 1995-96, but will not be available in FY 1996-97. These items are summarized in Table 1. Increasing the amount of the income tax that is earmarked to the SAF, would have a negative impact on the GF/GP budget. While the GF/GP grant to the SAF, which will total $589.1 million in FY 1995-96, would be able to be eliminated, GF/GP revenue would be reduced by $929 million due to the increase in the earmarking. As a result, the GF/GP budget would experience a net negative impact of $339.9 million. This estimated impact on the GF/GP budget is summarized in Table 2.

Table 1

FY 1995-96 School Aid Budget
Items That Could be Replaced with Increased
Income Tax Earmarking Proposed in HB 4657
(millions of dollars)

Carry-forward Balance from FY 1994-95	$283.5
General Fund Grant	589.1
Excess Lottery Revenue Transfer	25.0
Health & Safety Fund Transfer	26.0
Subtotal	$923.6
Addendum:	
HB 4657 estimated increase in income tax earmarking	$929.0

Table 2

Impact of House Bill 4657
on FY 1995-96 GF/GP Budget
(millions of dollars)

Existing Income Tax Earmarking -14.4%	($916.2)
H.B. 4657 Income Tax Earmarking - 29.0%	(1,845.2)
Proposed New Earmarking to SAF	(929.0)
Eliminate General Fund Grant to SAF	589.1
Net GF/GP Budget Impact	($339.9)

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