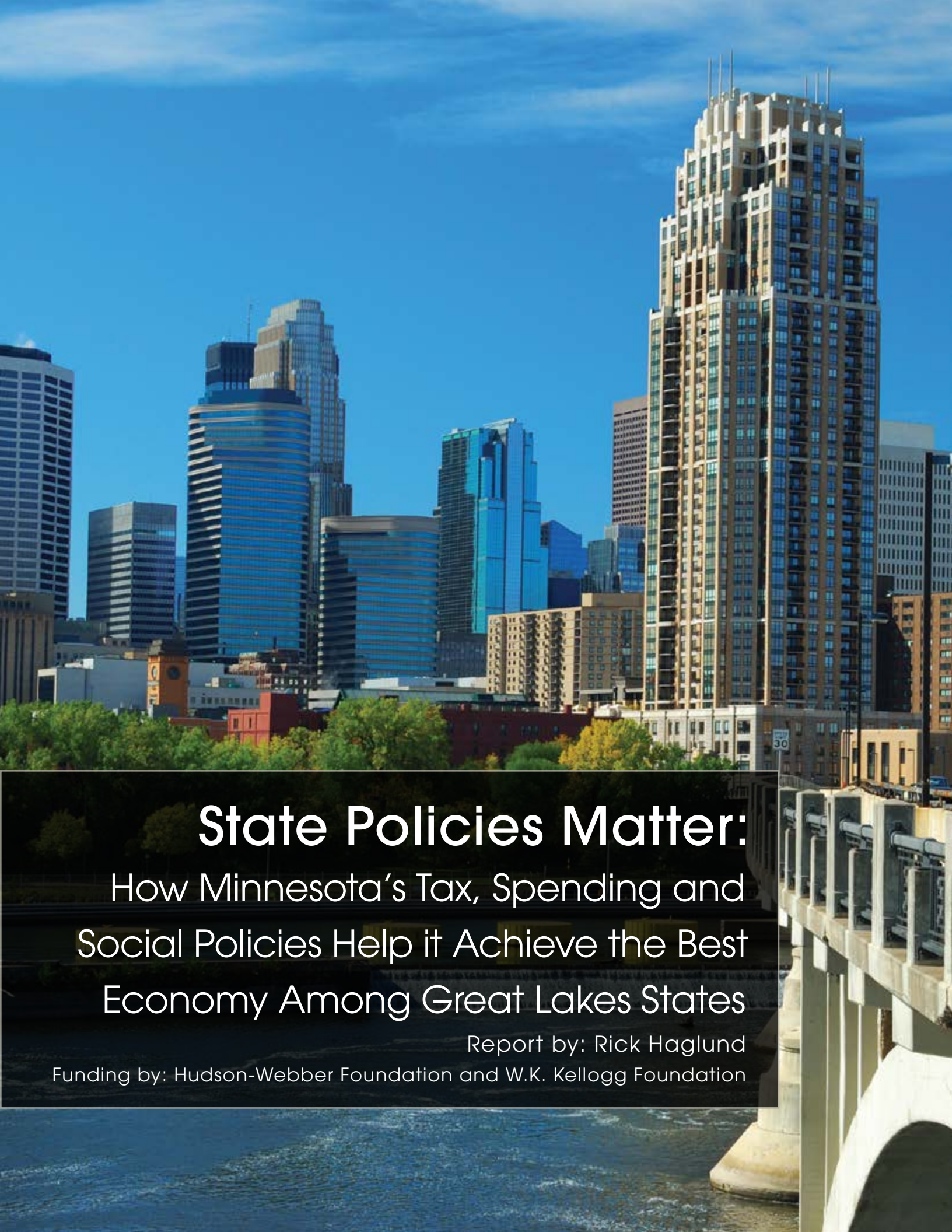

State Policies Matter:

How Minnesota's Tax, Spending and Social Policies Help it Achieve the Best Economy Among Great Lakes States

Report by: Rick Haglund

Funding by: Hudson-Webber Foundation and W.K. Kellogg Foundation

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Welcome

This report is a major departure for Michigan Future.

To date our research has focused almost exclusively around economic and demographic data. This report is about state policy.

We are moving into policy research largely in response to questions we get from those who read our reports and/or hear presentations on that work. The most frequent question we get is: "What are the most prosperous states and regions doing different than us?"Rather than developing a policy agenda, we have chosen to approach policy through case studies of economic growth-related policies in the most prosperous states and regions.

For years we have used Minnesota as a comparison state. Because it is a Great Lakes state (taking weather and the excuse that Michigan can't be like the coasts off the table) and it has enjoyed the best economic outcomes, by far, in the Great Lakes. It was the obvious choice for our initial policy case study.

In our last report, *The New Path to Prosperity: Lessons for Michigan from Two Decades of Economic Change*, we detailed the starkly different economic fortunes of Minnesota compared to Michigan since 1990. Minnesota is more than a Great Lakes success story. On most economic measures it is a national leader. And what makes it a national leader is characteristic of the most prosperous states around the country, except for the few states with energy-driven economies.

We asked Rick Haglund to do this initial case study for us. For decades Rick has been one of, if not, the best journalist covering the Michigan economy. He brings to this assignment a deep understanding of how state economies work and the role policy plays in shaping the economy. We asked Rick, of course, to investigate the tax and spending policies of Minnesota compared to Michigan. These are the policy levers widely considered to influence state economic outcomes the most. Tax and spending policies are the main focus of the report.

In doing that work the question arose: "How to measure tax burden?" The answer effects the comparison between the path Minnesota has chosen compared to Michigan. Two metrics are commonly used: per capita and as a percent of personal income. We decided to use both in the report. (As we did the last time we addressed the subject in our 2005 *A New Agenda for a New Michigan* report).

Here is why.

Percent of personal income is a measure of ability to pay for public goods and services. Per capita probably is the best metric of political will to pay for public goods and services. The fact that you have more income to pay for more public goods and services doesn't mean that you will. Taxes are a choice.

In 1992 when per capita income was close between the two states—Minnesota 15th and Michigan 20th—Minnesota state and local taxes combined were $357 (17%) per capita higher than Michigan ($2,488 to $2,131). So both states could "afford" about the same level of taxes but Minnesota chose to buy more public goods and services. Including in categories like education and infrastructure that we describe as public investments.

We also asked Rick to tackle two additional topics. First, regionalism in metro Minneapolis. The difference in economic outcomes between Minnesota and Michigan can largely be explained by the superior performance of metro Minneapolis compared to metro Detroit and metro Grand Rapids. For years, Minneapolis' approach to regionalism—particularly tax base sharing—has been viewed as a major ingredient in that region's economic success.

Michigan Future has identified being welcoming to all as a core component of prosperous states and regions. So we asked Rick to also investigate Minnesota's approach to being welcoming.

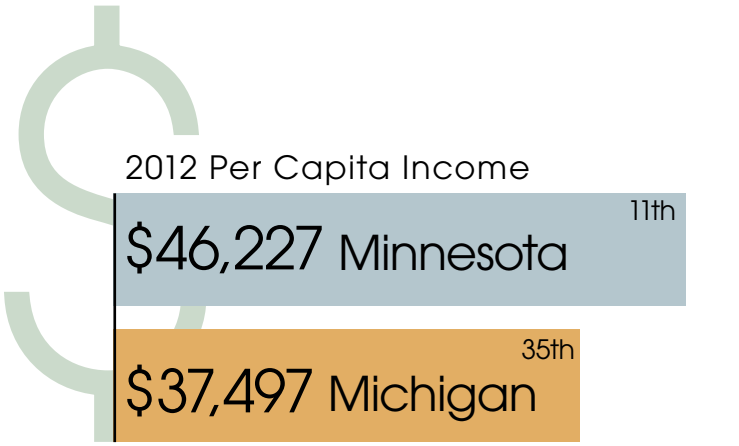
We are excited about the report Rick has produced. Our hope is that it will expand the conversation in Michigan and its regions about what economic policy should be to return Michigan to prosperity in an economy being transformed by globalization and technology. Minnesota, as you will see, has taken a different path to prosperity. At the very least, we hope Michiganders are open to exploring whether that path might work for us as well.

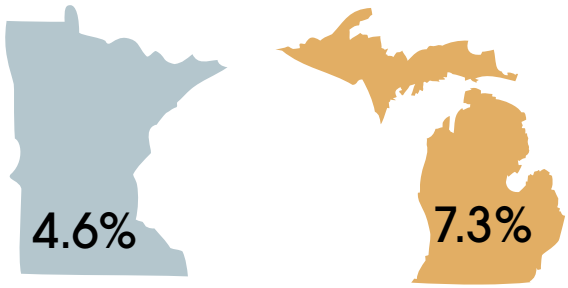
Lou Glazer
President, Michigan Future, Inc.

MICHIGAN FUTURE INC.
Helping create a prosperous Michigan

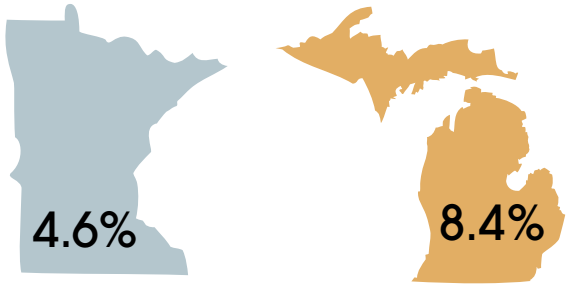
Introduction

Michigan and Minnesota



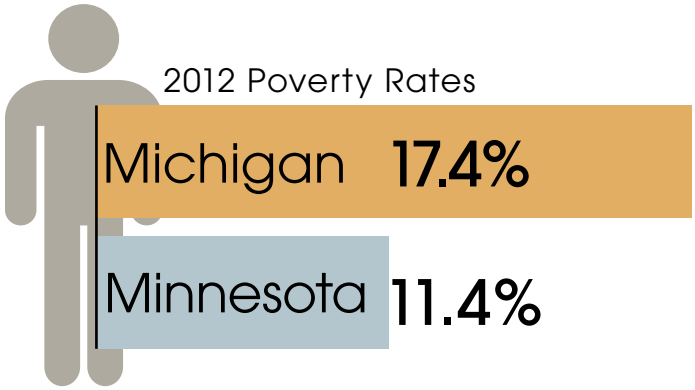


December 1993 Unemployment Rates



December 2013 Unemployment Rates

Minnesota had the ninth lowest unemployment rate in the country while Michigan had the fourth highest jobless rate among the states in December, 2013.



Michigan and Minnesota have a shared history as northern states settled by northern European and Scandinavian immigrants with economies defined by their proximity to the Great Lakes. Many people today continue to think of these two states as being quite similar. Indeed, Michigan and Minnesota are noted for their rugged natural beauty, pristine lakes and streams, pleasant summers and cold, snowy winters.

Up until about 20 years ago, living standards in the two states were similar, as well. In 1993, real per capita income of Minnesotans was only $555 a year more than that of Michigan residents. But since then that spread has widened considerably. In 2012, Minnesota's real per capita income was $46,227, or $8,730 more than Michigan's per capita income of $37,497.

We used Census Bureau population estimates from 2012 in calculating taxes per capita and spending per capita in this report.

Minnesota is the wealthiest state in the Great Lakes region and ranks 11th highest in the country in per capita income, which Michigan Future believes is the most important indicator of a prosperous state economy. Michigan ranks 35th in that measure. Unemployment rates in the two states tell a similar story. Michigan's jobless rate stood at 7.3 percent in December of 1993 and 8.4 percent last December.

Jobless rates in Minnesota have been far lower than in Michigan during that period. Minnesota's unemployment rate was the same last December as it was in December 1993 at 4.6 percent. Minnesota had the ninth lowest unemployment rate in the country while Michigan had the fourth highest jobless rate among the states in December.

Indiana has long been praised by conservatives for its low-tax, small-government, anti-union philosophy. But the Indiana model has not been a path to prosperity for its citizens. Indiana ranked 39th in the country with per capital income of $36,902 in 2012. Twenty years ago, Indiana had the 27th highest per capita income in the country.

Minnesota has consistently ranked among the 15th wealthiest states in the country annually since 1990.

In 2012, 15.6 percent of Indiana's residents lived in poverty, compared to just 11.4 percent of Minnesota residents living below the federal poverty line, according to new Census Bureau figures. Michigan's poverty rate was 17.4 percent in 2012.

Minnesota's recent economic performance is no fluke, either. The state has never had a month during the past 37 years in which the unemployment rate jumped into double-digit territory, according to Bureau of Labor Statistics data going back to 1976. And Minnesota has consistently ranked among the 15th wealthiest states in the country annually since 1990. It's clear that if Michigan is to regain the prosperity it enjoyed decades ago when the auto industry here reigned supreme, the state must aspire to be more like Minnesota than Indiana.

How has Minnesota achieved such an enviable record of economic success? Part of the answer lies in the state's rich mix of knowledge-based industries that pay workers higher wages than in Michigan. Minnesota also is highly successful in keeping and attracting college graduates. It's the region's leader and a top 15 state in that ranking, which tracks closely with personal income. But underpinning Minnesota's private-sector success are tax, spending and other public policies that promote economic growth, as well as stability through the ups and downs of the business cycle.

Minnesota's sustained, strong economy defies the conventional wisdom that low taxes are the singular path to prosperity. The state's taxing and spending priorities reflect Minnesota's long-held belief that support for education from preschool to the university level, and high-quality government service are key ingredients in producing prosperity of its citizens. This report outlines those policies and offers an economic road-map for serious consideration by Michigan citizens and policy makers.

I. It's More Than "Minnesota Nice"

Three decades of Minnesota Governors

Republican Governor Arne Carlson and Governor Tim Pawlenty

Independent Governor Jesse Ventura

Democratic Governor Mark Dayton

Minnesotans have long been known for their pleasant demeanor and respectful attitudes toward others.

Many say those views were shaped by Scandinavian settlers who believed that individual pursuits should be balanced with investments that promote the public good.

"It's an ethic that is difficult to articulate, but plays a very real role in public policy here" said Mark Haveman, executive director of the Minnesota Center for Fiscal Excellence, a sister organization to the nonpartisan Citizens Research Council of Michigan. Dane Smith, who worked as a political journalist in Minnesota for 30 years and now heads the progressive public policy think tank Growth & Justice in St. Paul, puts it this way:

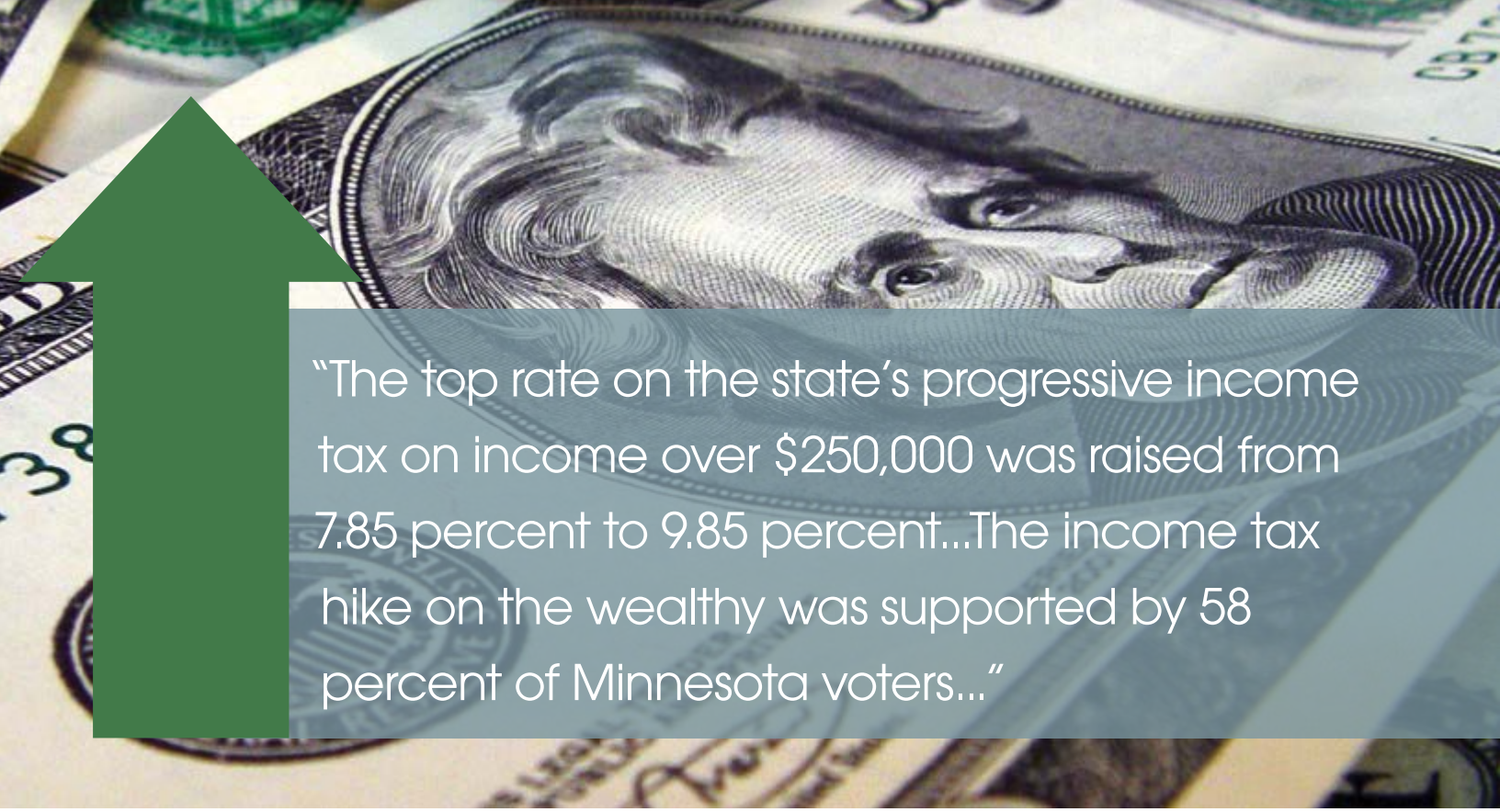
"Minnesota has a 150-year tradition of public-mindedness, and investment in human capital and physical infrastructure that is central to our success," he said. "We have higher taxes and bigger government, but better government than most states."

The state's tax and spending policy framework was set in the early 1970s. It's called the "Minnesota Miracle." The core of the strategy is shifting more of the burden of financing schools and local government—primarily cities—from escalating local property taxes to the state income and sales taxes. Many in the state see the Minnesota Miracle as setting the stage for investment in education, communities and transportation that created a climate for strong economic growth.

While Minnesota's state politics have long been dominated by the Democratic Party—it's known there as the Democratic Farmer-Labor Party—the state's tax structure has been remarkably stable throughout changes in political control of state government. Four governors representing three political parties—Republicans Arne Carlson and Tim Pawlenty, Independent Jesse Ventura and current Democratic Gov. Mark Dayton—have led the state over the past three decades.

Democrats, who currently control the Legislature and the governor's office, have enjoyed majorities in both houses during 10 of 16 two-year legislature sessions since 1983-1984. They also controlled the Legislature and the governor's office four times in that period. The only time Republicans have controlled both houses was in the 2011-2012 session. They have not controlled the Legislature and the governor's office at the same time since 1969.

As in other states, Minnesotans are engaged in a debate over the optimal level and type of taxation to promote future growth. But Haveman says there is wide agreement that the state's "foundational competitiveness," which includes investment in education, transportation and other infrastructure spending that promotes a strong quality of life, is key to Minnesota's continued prosperity.



Indeed, Minnesota in 2013 addressed a budget deficit by raising taxes dramatically on the wealthy and businesses in the state, part of a tax package expected to raise $2.1 billion over two years to eliminate a budget deficit and boost investment in education, transportation and other areas. The top rate on the state's progressive income tax on income over $250,000 was raised from 7.85 percent to 9.85 percent. Business taxes were also increased slightly. The measures were proposed by Gov. Dayton and supported by the Democratic majority in the Legislature.

Raising taxes at the state level is the centerpiece of a plan to restore Minnesota's long-held fiscal philosophy of having state taxes represent a larger share of the overall state-and-local tax burden. Local taxes rose under Pawlenty's administration because of tax cuts at the state level.

The income tax hike on the wealthy was supported by 58 percent of Minnesota voters, according to a statewide poll in June 2013 by the Minneapolis Star-Tribune. Views on the tax hike broke across party lines, with 90 percent of Democrats supporting it and 76 percent of Republicans saying they were opposed to the tax hike. Gov. Mark Dayton's garnered a 57 percent approval rating in that poll, the highest level in Dayton's nearly three years as governor.

Faced with a deficit after taking office in 2011, Michigan Gov. Rick Snyder, a Republican, took a very different approach. He cut business taxes, raised revenue by taxing pensions and cutting back on the state's Earned Income Tax Credit for low-income families, and slashed support for higher education and cities. Snyder and the Republican-controlled Legislature have since restored some funding for education and cities as the state's auto-driven economy bounced back from a deep recession. But he and the Legislature have proposed more tax cuts.

The different approaches to addressing budget issues—Michigan tightening spending and cutting taxes for business and, effectively, the wealthy, while Minnesota raised taxes on the wealthy and businesses to invest even more in public services—typifies the varying strategies two states have utilized in addressing fiscal and economic development policies over the last 20 years.

The impact of those differences in a nutshell: The Minnesota tax boost will help fund additional spending on higher education—enough so that there will be no tuition increases at public universities in Minnesota for the next two years. Meanwhile, state support for Michigan universities today is lower than it was in 2010, with resulting tuition increases needed to sustain quality educational opportunities.

Two very different strategies, with advocates for both claiming the goal of more and better jobs.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Feb $87,490.00 $9,472,651.02 $89
Mar $2,874.98 $847,592.00 $18
Apr $8,923,897.00 $62,934,875.00 $4
May $8,374.98 $27,664,313.76 $87
Jun $849,571.88 $88,409,178.00 $16
Jul $4,409,284.00 $7,716,354.22 $88
Aug $837,450.00 $849,576.09 $55
Sep $2,284,761.00 $102,843,675.00
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II. Taxes

Taxes Per Capita

State Taxes

$3,880 Minnesota

$2,535 Michigan

2011 Combined State and Local Taxes

$5,016 Minnesota

$3,655 Michigan

Taxes as % of Personal Income

2013 State Taxes

8.3% Minnesota

6.6% Michigan

2011 Combined State and Local Taxes

11.9% Minnesota

10.6% Michigan

Minnesotans—both individuals and businesses—pay higher tax rates than Michiganders.

When it comes to how much tax revenue was collected in 2013 by the state alone and 2011 (latest available) in state and local combined Minnesotans pay higher taxes than Michiganders. Using data from the Census Bureau, the Federation of Tax Administrators calculates in 2013 Minnesota collected $3,880 per capita in state taxes and in 2011 $5,016 per capita in combined state and local taxes. In Michigan tax collections on the same measures were $2,535 and $3,655.

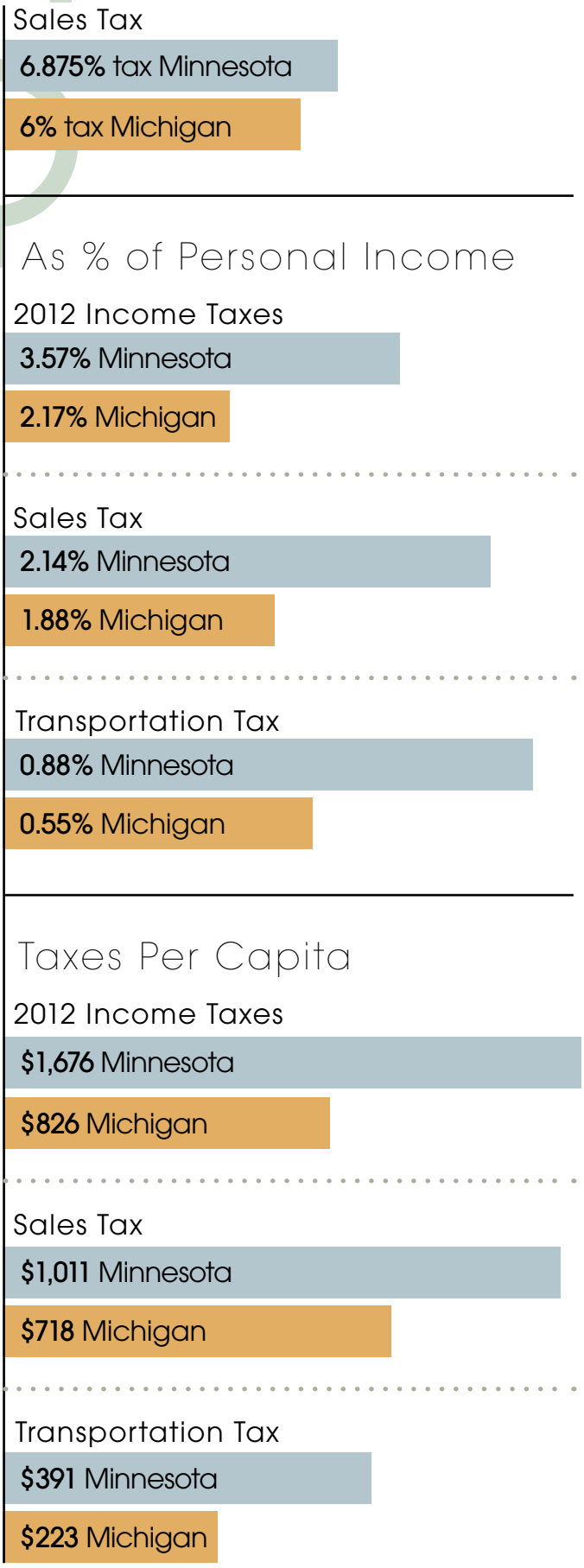
Using the same data, the Federation of Tax Administrators calculates in 2013 Minnesota state taxes were 8.3 percent of personal income and in 2011 11.9 percent in combined state and local taxes. In Michigan taxes on the same measures were 6.6 percent and 10.6 percent. If Michiganders had paid the same state taxes per capita as Minnesotans, Michiganders would have paid $13.4 billion more in 2013. If Michiganders had paid the same state taxes as a percent of personal income as Minnesotans, Michiganders would have paid $6.5 billion more in 2013.

The oft-cited Tax Foundation rankings of state taxes support the data that Minnesota is a higher tax state than Michigan. Minnesota saw its tax climate ranking by the Tax Foundation drop from 41st in 2009 to 47th in 2014, while Michigan saw its ranking increase from 21st to 14th over that period.

Personal Income Taxes

Minnesota has long had a progressive state income tax system in which its richest residents pay a higher percentage of their income in taxes than do its poorest residents. That's unlike in Michigan, where everyone pays a flat 4.25 percent rate. Between 2000 and 2012, Minnesotans paid

Tax	Minnesota Rates	Michigan Rates
Income	5.35% – 9.85%	4.25%
Sales (State and Local)	6.875% – 7.875%	6%
Gasoline	28.6¢/gallon	19¢/gallon
Corporate Income Tax	9.8%	6%



between 5.35 percent and 7.85 percent of their income in personal income taxes.

In 2013, joint filers earning a maximum $35,480 paid the bottom 5.35 percent rate, while joint filers earning between $35,481 and $140,960 paid 7.05 percent. Those filing jointly and earning more than $140,960 paid 7.85 percent of their income in taxes. Last year, the Minnesota Legislature boosted the top rate to 9.85 percent for joint filers on income more than $250,000.

As in Michigan, pension income in Minnesota is taxed at the applicable personal income tax rate.

In 2013, Minnesota residents paid $9.0 billion in personal income taxes. That is $1,676 per person and 3.57 percent of personal income. Michigan residents paid $8.2 billion in personal income taxes—$826 per person and 2.17 percent of personal income.

Minnesota also has one of the most generous earned income tax credits (EITC) for low-income wage earners in the country. Minnesota's refundable credit ranges from 25 percent to 45 percent of the federal credit, averaging 33 percent of the federal credit, according to the Internal Revenue Service.

Michigan's EITC was cut from 20 percent to 6 percent of the federal credit in 2011 and is among the lowest rate of the 26 states with a state EITC.

Sales Tax

Minnesota's sales tax rate is 6.875 percent, compared to Michigan's rate of 6 percent. Local governments are allowed to assess a sales tax of up to 1 percent on top of the state sales tax. Depending on where they live, Minnesotans can pay a sales tax rate as high as 7.875 percent.

State and local sales taxes produced $5.4 billion in revenue last year, including $330 million in local sales taxes. That is $1,011 per capita and 2.14 percent of personal income. Michigan's sales tax raised $7.1 billion in 2013, amounting to $718 per capita and 1.88 percent of personal income.

In 2008, Minnesota voters approved boosting the sales tax to 6.875 percent for 25 years. Voters also adopted a requirement that a 0.375 percent share of the tax be allocated for spending on wildlife protection, water quality, parks and trails, and art and culture.

Transportation/Gas Tax	Minnesota	Michigan
Gas Tax	28.6¢/gallon	19¢/gallon
Diesel Tax	28.6¢/gallon	15¢/gallon

Minnesota's sales tax on motor vehicles is 6.5 percent, with the revenue dedicated to transportation funding. Sixty percent of the revenue raised goes to the state's highway fund, while 40 percent is allocated to public transit. Vehicles are taxed on the difference between the purchase price of the car or truck and the value of a trade-in vehicle.

Sales taxes in Michigan and Minnesota are mostly limited to the purchases of goods. But Minnesota taxes many services exempt from the sales tax in Michigan, including membership and admission fees to workout facilities, the labor to install various products, mainly on business-to-business transactions and landscape work. A full list is at the end of this report. Michigan passed and then rescinded sales taxes on many services several years ago after a general outcry by affected businesses.

Michigan and Minnesota tax telecommunications services, lodging, electricity and home heating fuels. Another significant difference between Michigan and Minnesota is that Minnesota exempts clothing from its sales taxes, while Michigan taxes clothing purchases.

Cigarette Taxes

Minnesota lawmakers also boosted the excise tax on cigarettes in 2013 from $1.23 to $2.83 a pack and indexed it to inflation. Minnesota also assesses a 51.2-cent sales tax on each pack. The excise tax is expected to raise more than $400 million in new revenue over the next two years, with some of it being used to fund early childhood education.

Minnesota now has the seventh-highest cigarette tax in the nation. Michigan's $2-a-pack excise tax is the nation's 12th highest, according to the Campaign for Tobacco-Free Kids. Michigan also assesses its 6 percent sales tax on cigarettes.

Transportation Taxes

Gasoline and diesel fuel are taxed at 28.6 cents a gallon (including a 0.1 cent fee) while E85 (15 percent gasoline and 85 percent ethanol) is taxed at 20.26 cents a gallon in Minnesota.

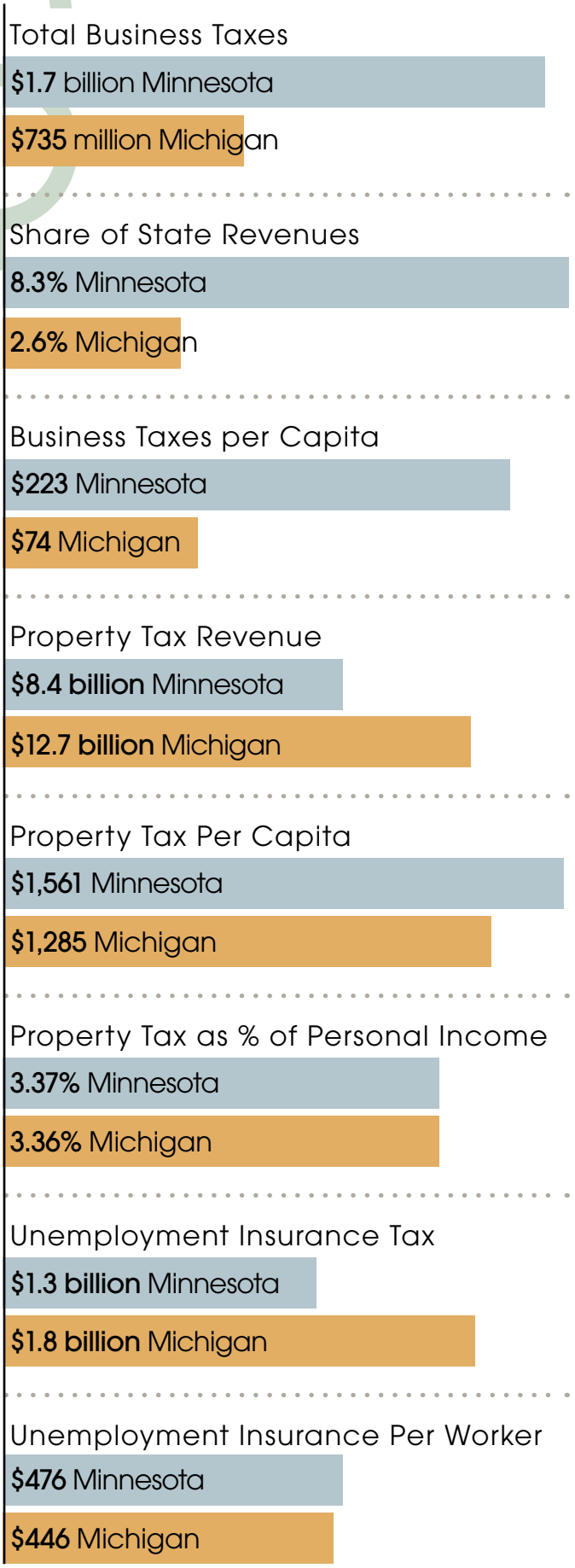
Minnesota boosted its sales tax on gasoline and diesel fuel from 20 cents a gallon to 25 cents a gallon in 2008 and tacked on a surcharge that was capped at 3.5 cents. Minnesota's gasoline tax is 9.6 cents a gallon higher than Michigan's gas tax. Liquefied petroleum gas for motor vehicle use is taxed at 21.35 cents a gallon while liquefied natural gas is taxed at 17.1 cents a gallon. Compressed natural gas is taxed at $2.474 per thousand cubic feet.

A third source of state funding for roads comes from a motor vehicle registration tax. Vehicles are taxed at 1.25 percent of their base value (the manufacturer's list price without options for new vehicles) plus a $10 fee. In future years the tax decreases based on a 10-year depreciation schedule. The state assesses a $35 flat fee for vehicles more than 10 years old.

Minnesota raised $2.1 billion from state transportation taxes in fiscal year 2013. Motor fuels taxes raised 46.6 percent of state transportation revenues, while 31.9 percent came from vehicle registration fees and 18.5 percent came from the motor vehicle sales tax in 2012. Three percent of highway tax revenues came from miscellaneous sources.

As part of the 2013 tax hike package, Minnesota boosted its "wheelage tax" from $5 a vehicle to $10 a vehicle and allowed all 87 counties in the state to collect it. Previously, the tax had been limited to counties in the Minneapolis-St. Paul metro area. Forty-seven counties levy the tax in 2014. The state collects the tax and distributes it to the appropriate county for road repair and expansion projects and public transportation.

Michigan relies mainly on its 19 cents-a-gallon gasoline tax, a 15 cents-a-gallon diesel fuel tax, a 15-cents-a-gallon liquefied petroleum tax and vehicle registration fees for the state's share of transportation funding. The state taxes gasoline containing at least 70 percent ethanol and diesel fuel containing at least 5 percent biodiesel at 12 cents a



gallon. (The state also imposes a sales tax on gasoline; however that money is not earmarked for transportation and instead funds schools and general fund functions).

Motorists pay registration fees based on the price of the vehicle. Fees decline by 10 percent a year until the fifth renewal. Michigan's vehicle registration fees vary from $33 to $148, according to the National Conference of State Legislatures.

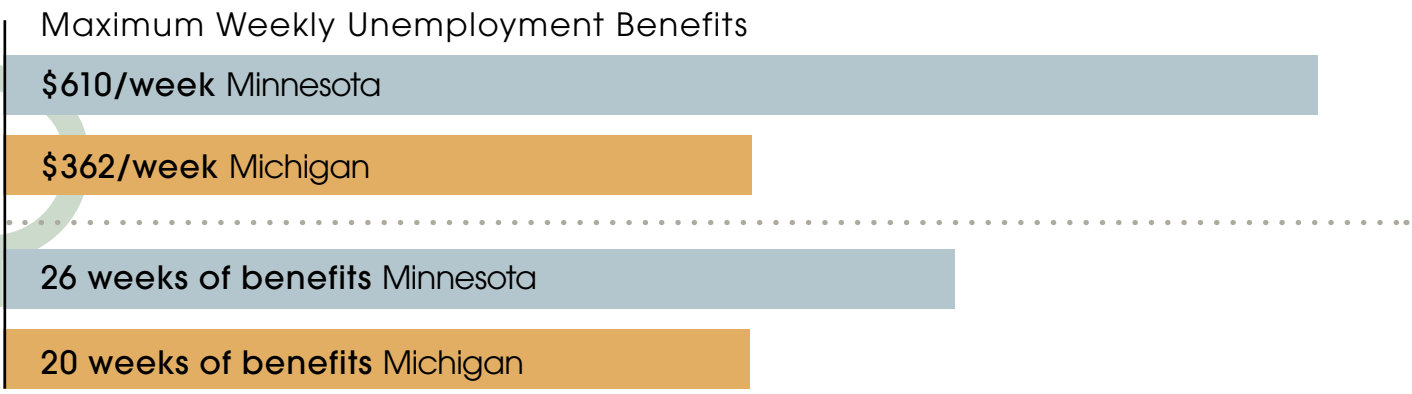
Michigan raised about $2.2 billion from state transportation taxes from state funds in 2013, slightly more than Minnesota's $2.1 billion. Minnesotans pay $391 per capita and 0.88 percent of personal income in transportation taxes. Michiganders pay $223 and 0.55 percent of personal income.

Business Taxes

Minnesota taxes businesses at a higher rate than does Michigan. And unlike in Michigan, most Minnesota businesses are subject to state corporate income taxation. "C" corporations—generally large shareholder owned operations—are taxed at a 9.8 percent rate (Minnesota calls its corporate income tax a "franchise tax"), compared to Michigan's 6 percent corporate income tax rate. Like Michigan, Minnesota assesses its corporate income tax only on "C" corporations. Partnerships, "S" corporations, limited liability companies and sole proprietorships are exempt.

Minnesota businesses with a combined value of property, payroll and sales exceeding $500,000 also pay a "minimum fee" ranging from $100 to $5,000. Business income passed through to shareholders of "S" corporations, partnerships, limited liability companies and sole proprietorships is taxed at the applicable personal income tax rate. Minnesota also assesses a "gross earnings tax" on insurance companies, hospitals, nursing homes, surgical centers and wholesale prescription drug distributors.

Minnesota insurance companies pay rates ranging from 1 to 3 percent on net premiums. Insurance companies in Michigan pay a gross premiums tax of 1.25 percent. Minnesota collected nearly $1.7 billion in business tax revenues last year, including $416 million in insurance premium taxes. That represents 8.3 percent of total state taxes of $20.5 billion. Michigan's net business tax revenues of $735 million, including the insurance company tax, comprised 2.6 percent of total state revenues of $27.8 billion in 2013.



For Michigan businesses to pay the same proportion of total state revenue as Minnesota, Michigan businesses would have paid $976 million more in 2013.

Property Taxes

Property in Minnesota, like in Michigan, is mostly taxed at the local level. But there is a state tax levied on commercial, industrial, public utility, railroad, mineral and seasonal recreational property.

State property taxes are assessed based on a percentage of the market value of parcels, multiplied by a "net class rate" that ranges from 0.4 percent to 2 percent, and multiplied again by the state tax rate. Commercial and industrial property owners paid a tax rate of 51.1 percent in 2012, while owners of vacation property paid a 20.75 percent tax rate.

Local property taxes are assessed in the same manner the state property tax is levied. But tax rates vary by locality. Local property taxes in Minnesota generated $7.7 billion in fiscal year 2013 while state property taxes generated about $817 million. Minnesota does not assess a tax on equipment, machinery and other personal property owned by businesses in the state. Michigan has passed legislation that will phase out its personal property tax by 2023 if voters approved the measure in August.

Michigan levies a 6 mill state education tax, or $6 per $1,000 of state equalized value, on real property to finance schools. State equalized value is 50 percent of true cash value. The state education tax generated about $1.8 billion while local property taxes produced about $10.9 billion in revenue primarily for local units of government in fiscal year 2013.

State and local property taxes in Minnesota raised $8.4 billion, or $1,561 per capita compared to $12.7 billion raised, or $1,285 per capita in Michigan. As a percent of personal income the two states are nearly identical. 3.37 percent in Minnesota compared to 3.36 percent in Michigan.

Unemployment Insurance Taxes and Benefits

Tax rates on unemployment insurance paid by employers vary widely, depending on their experience laying off employees. Those with a long record of layoffs typically pay a much higher tax rate than those who have never laid off employees.

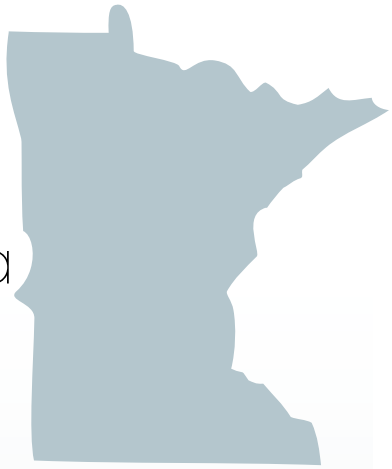
Employers in Minnesota paid $1.3 billion in unemployment insurance taxes in 2012 compared to $1.8 billion paid by Michigan employers, according to a 2013 study by Ernst & Young and the Council on State Taxation. That works out to about $476 per worker in Minnesota compared to $446 per in Michigan.

Unemployment insurance taxes comprised 10.7 percent of all state and local business taxes paid in 2012 by Minnesota employers, according to the study. Unemployment insurance taxes represented 12.8 percent of business taxes paid by Michigan employers. Minnesota is far more generous than Michigan in state unemployment benefits paid to laid-off workers. Minnesota workers can receive as much as $610 a week in benefits for 26 weeks.

In 2011, Michigan trimmed the number of weeks laid-off workers can collect benefits from 26 weeks to 20 weeks. Michigan's maximum weekly benefit is $362, 58 percent less than Minnesota's maximum.

III. Minnesota's Spending Priorities

Total State Spending



Minnesota

Total State Spending

2013: $23.9 billion

2013 Spending Per Capita

$4,443 Minnesota

$2,813 Michigan

Michigan

Total State Spending

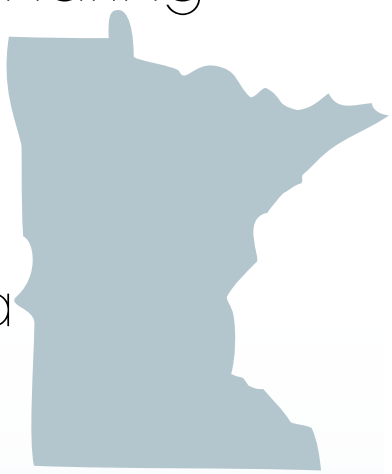
2013: $27.8 billion

There's no question that Minnesota is a high-tax, high-expenditure state. Spending from state resources totaled $23.9 billion in fiscal year 2013, or $4,443 per capita, according to Minnesota Department of Management and Budget. That was $1,630 per capita more than in Michigan, which spent $27.8 billion from state resources, according to state Senate Fiscal Agency data.

But Minnesota's taxes pay for investment priorities that state policymakers have long believed are critical to Minnesota's prosperity. The state's top priorities include funding for education from preschool through college, human services, transportation and local government. In addition to higher tax revenue Minnesota also is able to fund those priorities at higher level than Michigan because of different budget priorities.

Here is a look at Minnesota's spending on priority investments:

Revenue Sharing



Minnesota

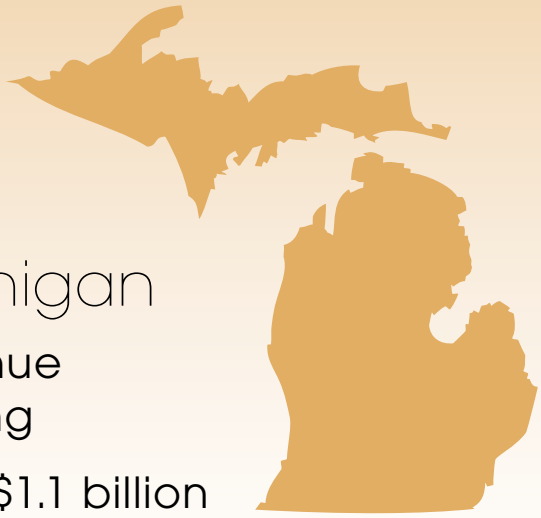
Revenue Sharing

2013: $2.4 billion
2013: $465 per capita

2014 Spending Per Capita

$468 Minnesota

$132 Michigan



Michigan

Revenue Sharing

2013: $1.1 billion
2013: $119 per capita

Revenue Sharing

Minnesota shares state revenue with cities, towns and counties under what is called the Local Government Aid program. The state also provides additional aid for local police and fire departments and a variety of other local services.

Minnesota instituted revenue sharing in the early 1970s as a central element of what became known as the "Minnesota Miracle," which shifted more of the burden of financing schools and local government—primarily cities—from escalating local property taxes to the state income and sales taxes.

Local aid declined over much of the past decade as former Republican Gov. Tim Pawlenty sought to shrink state spending by cutting state support for cities (a strategy that has been used in Michigan, too).

Minnesota appropriated $593.1 million in aid to cities and counties in fiscal year 2013. Due in large part to the recent tax increase revenue sharing saw a big increase in fiscal year 2014. Minnesota's fiscal year 2014 budget provides $80 million of additional aid to cities and another $40 million to counties, for a total of $713 million, an increase of 20.2 percent. Overall, Minnesota provided state aid of $2.4 billion to local governments in 2013. Michigan has a two-part revenue sharing program that includes payments mandated by the state constitution and state statute.

Michigan is boosting total state revenue sharing from $1.1 billion in 2013 to $1.13 billion in the current fiscal year, according to the state Senate Fiscal Agency. That represents a 4 percent increase in revenue sharing. But that's only a small restoration of the cuts of the last decade in state support for Michigan cities.

The Michigan Municipal League estimates that the state's failure to fully fund revenue sharing has resulted in more than $4 billion in revenue sharing cuts to cities, townships and villages since 2001. Minnesota spent $465 per capita on aid to local governments in 2013, while Michigan spent $119 per capita. In 2014, that increased to $468 in Minnesota and $132 in Michigan.

Higher Education

Minnesota

Higher Education Spending:

2013: $1.3 billion

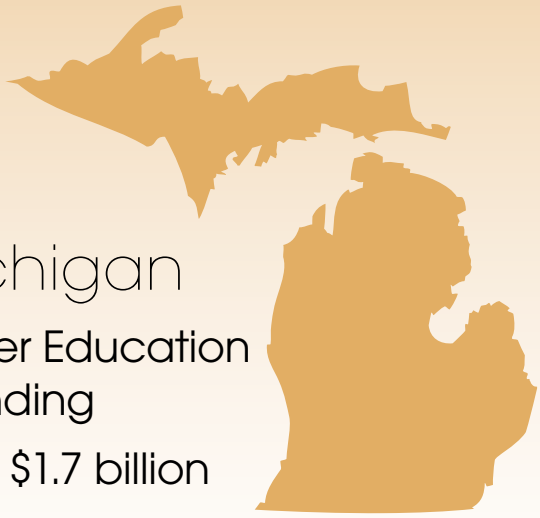
Ranked #10 for Education Attainment

(33% of the population have a bachelor's degree or above.)

2013 Spending Per Capita

$242 Minnesota

$172 Michigan



Michigan

Higher Education Spending

2013: $1.7 billion

Ranked #36 for Education Attainment

(26% of the population have a bachelor's degree or above.)

Higher Education

Minnesota, a state with about 55 percent of the population of Michigan, spent about 75 percent as much as Michigan did on universities and community colleges in the 2013 fiscal year.

Michigan spent about $1.7 billion on higher education and community colleges while Minnesota spent about $1.3 billion, mostly for the University of Minnesota and the 31 community colleges and state universities in the Minnesota State Colleges and Universities system. That works out to $242 per capita in Minnesota compared to $172 per capita in higher education spending in Michigan.

Minnesota is spending an additional $98 million on higher education in the current fiscal year compared to 2012–13, and has budgeted another $29.1 million increase on top of that in the 2015 fiscal year. In exchange, the state's colleges and universities will freeze tuition through 2015. Michigan is spending an additional $33 million on higher education in the current fiscal year; Gov. Snyder has proposed an additional $80 million for the 2014–15 fiscal year.

Minnesota's investment in higher education—and its ability to retain those grads and attract more—has resulted in the state having one of the most highly educated work forces in the country, a clear advantage in a growing knowledge-based economy. In 2012, 33.2 percent of Minnesotans had a bachelor's degree or above, the 10th highest in the nation. Michigan ranked 36th in the country with 26.0 percent of its residents having a bachelor's degree or above.

Early Education

Minnesota

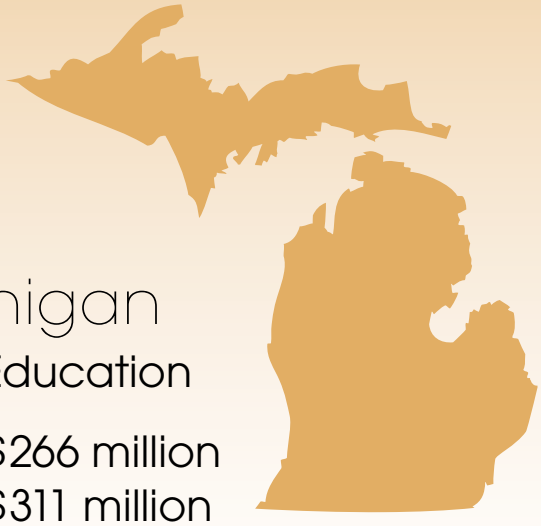
Early Education Spending

2013: $153 million
2014: $183 million

2013 Early Education Spending Per Capita

$28 Minnesota

$27 Michigan



Michigan

Early Education

2013: $266 million
2014: $311 million

Early Childhood Education

Minnesota was a pioneer in early childhood education. In 2006, business leaders in the state agreed to fund a $20 million project, called the Minnesota Early Learning Foundation. The foundation conducted research, established a rating system for early learning programs and funded a pilot scholarship project for low-income children in St. Paul. The project ended in 2011, but was replaced with a new business-led organization, called Parent Aware for School Readiness that promotes the rating system now overseen by the Minnesota Department of Education.

Scholarships are awarded for students to attend only four-star rated programs run by the private sector and public school systems. Last year, Minnesota spent $153 million from state resources on preschool and childcare assistance, and is spending $183 million this year.

Michigan also has increased early childhood education funding. Last year, the state boosted funding for its Great Start Readiness preschool program by $65 million, more than any other state. Michigan spent $266 million last year for preschool and childcare assistance and boosted funding this year to $311 million. In 2013 Minnesota spent $28 per capita on early childhood programming compared to $27 in Michigan.

K–12 Spending

Minnesota

K–12 Spending

2013: $11.1 billion

(Including $2.3 billion in local funding.)

K–12 Education

Minnesota funds K–12 education through the state's general fund, and local property tax levies. K–12 funding last year totaled $11.1 billion, including nearly $2.3 billion in local property taxes.

Michigan spent about $14.6 billion for K–12 funding in the 2013 fiscal year, including $3.4 in local funds. Minnesota spent $2,067 per capita on K–12 education in 2013, while Michigan spent $1,447 per capita. Minnesota's investment in K-12 education appears to be paying off in students who are among the most prepared in the country to attend college.

Last year's graduating seniors in Minnesota posted an average composite score of 23.0 on the ACT test, the highest in the nation among the 28 states in which more than half the college-bound students took the test in 2013. Minnesota has led the nation in average composite ACT scores for eight consecutive years. The national composite score last year was 20.9.

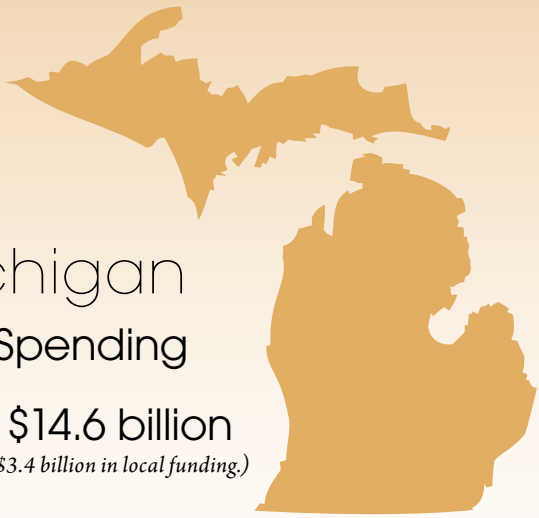
Thirty-nine percent of Minnesota students were deemed college-ready in all four subjects in the ACT, among the best in the country. In Michigan, twenty-one percent of students were considered college ready.

All high school students in Michigan are required to take the ACT test. About 74 percent of Minnesota's 2013 graduating class took the ACT, according to the Minnesota Office of Higher Education, which almost certainly contributes to Minnesota's better outcomes.

2013 K–12 Spending Per Capita

$2,067 Minnesota

$1,447 Michigan



Michigan

K–12 Spending

2013: $14.6 billion

(Including $3.4 billion in local funding.)

Health and Human Services

Minnesota

Public Assistance Spending

2013: $6.4 billion

2013 Health and Human Services Spending Per Capita

$1,134 Minnesota

$617 Michigan

Michigan

Public Assistance Spending

2013: $6.1 billion

Health and Human Services

Minnesota has long provided a strong safety net for the poor and those who have fallen on hard times with generous spending on health and human services. Minnesota spent $6.4 billion in 2013 while Michigan spent $6.1 billion. Minnesota's spending amounted to $1,134 per person compared to Michigan's spending of $617 per capita on health and human services.

Minnesota spent $8,680 per person on public welfare for those below 200 percent of the federal poverty line, more than any other state except Alaska, according to a March 2013 study by the Center of the American Experiment, a conservative think tank in Minneapolis. Michigan spent just under $4,000 per person. Minnesota limits lifetime cash assistance welfare benefits to 60 months, in line with federal law. Michigan trimmed its lifetime limit to 48 months in 2011.

Corrections

Minnesota

Corrections Spending

2013: $490 million

2013 Corrections Spending Per Capita

$91 Minnesota

$202 Michigan

Michigan

Corrections Spending

2013: $2 billion

Public Safety

One area where Minnesota spends less overall than Michigan on a per capita basis is in public safety, including corrections. And it spends substantially less on building and operating prisons, expenses that many states would like to reduce to allow for more spending in areas such as education and infrastructure improvements.

Overall, Minnesota spent $186 per capita on public safety last year, including prisons and police. That compared to $212 in Michigan. But Minnesota spent just $490 million of its $1.0 billion public safety budget in 2013 on prison operations and construction in 2013, according to an estimate by the National Association of State Budget Officers.

In Michigan, $2 billion of the state's $2.8 billion in public safety spending funded corrections. Minnesota spent $95 per capita to fund police and the judiciary in 2013 compared to Michigan's spending of $81 per capita.

The rate of violent crimes in Minnesota is half of Michigan's rate, according to 2012 data, the latest available from the FBI. Minnesota had a violent crime rate of 230.9 incidents per 100,000 residents, compared to 454.5 violent crimes per 100,000 residents in Michigan.

Transportation

Minnesota

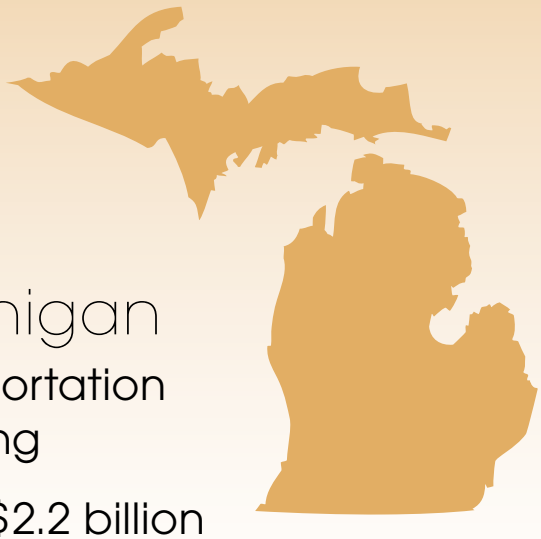
Transportation Funding

2013: $2.7 billion

2013 Transportation Spending Per Capita

$502 Minnesota

$223 Michigan



Michigan

Transportation Funding

2013: $2.2 billion

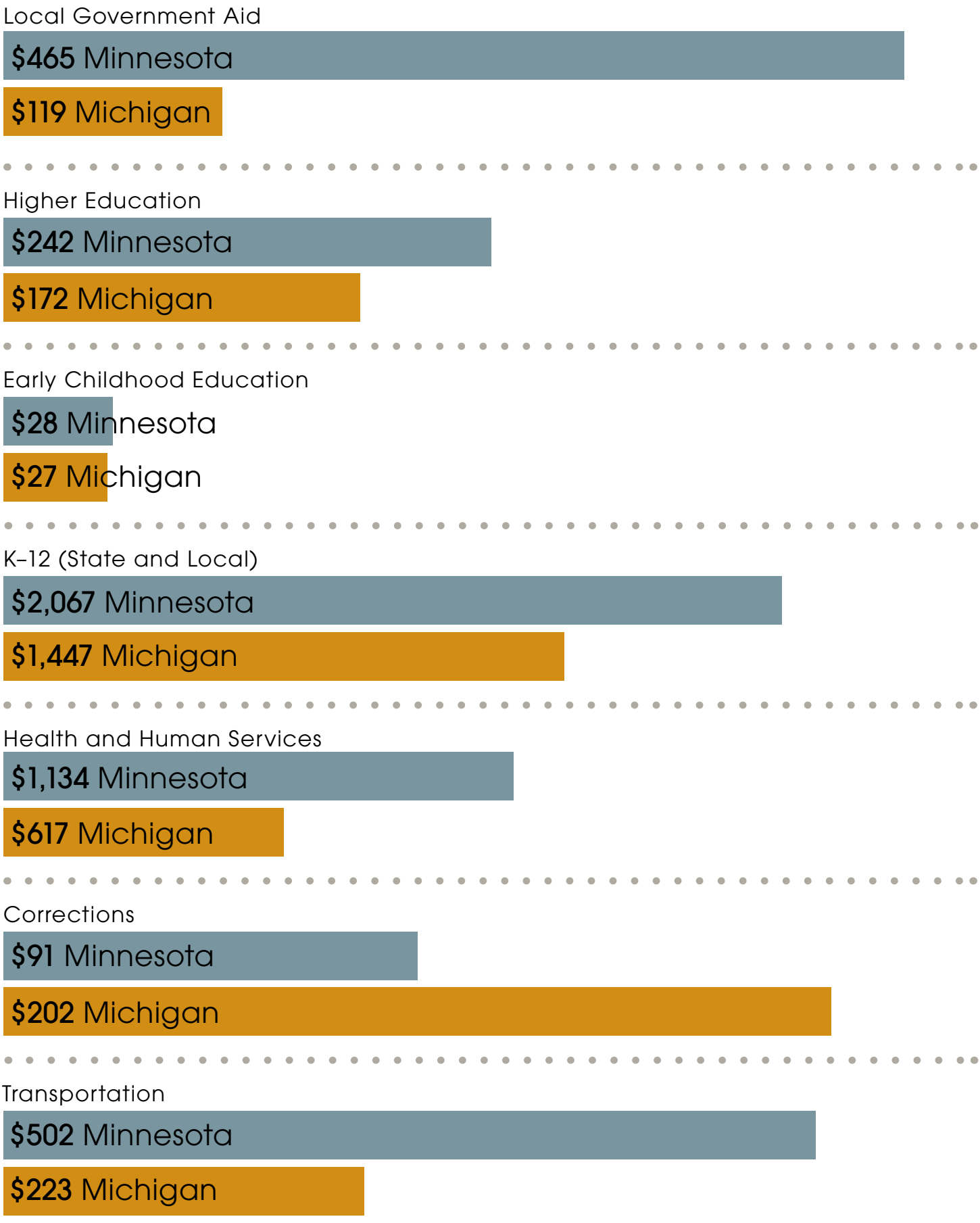
Transportation

Minnesota spent about $2.7 billion in state funds for roads and public transit in the 2013 fiscal year, some $500 million more than the $2.2 billion Michigan spent on transportation funding, according estimates by the National Association of State Budget Officers. On a per capita basis, Minnesota spent $502 while Michigan spent $223 on transportation.

Michigan will spend slightly more from state resources in the 2013-14 fiscal year due to a special $121.3 million appropriation from the state's general fund. But the Legislature has so far rejected Gov. Rick Snyder's efforts to raise an additional $1.2 billion through higher gasoline taxes and vehicle registration fees.

Funding for state roads in Minnesota will increase by about $360 million through 2015 as part of the state budget adopted in May by the state legislature. The state also appropriated $37 million in fiscal year 2013 toward the state's 10 percent share of constructing a new light rail line between downtown Minneapolis and suburban Eden Prairie. And it budgeted another $18 million to the Metropolitan Council for bus, light rail and commuter operations in the Twin Cities. In future years, the annual appropriation will be $11.7 million.

2013 Per Capita Spending in Key Areas



IV. Regionalism in the Twin Cities

The Minnesota Legislature established the Metropolitan Council in 1967 as the regional planning agency serving the seven-county Minneapolis-St. Paul metro area.

It's similar to the Southeast Michigan Council of Governments (SEMCOG), but with a much broader mandate and taxing powers. In addition to long-range planning, the Metropolitan Council operates Metro Transit, which last year served 81 million bus and rail passengers, and operates the metro area's wastewater treatment system.

A 17-member policy board governs the Metropolitan Council. But unlike SEMCOG, board members cannot be local government officials and are appointed by the governor. Local officials serve on various Council advisory committees, though.

Forty-seven percent of 2014's $887.8 million budget comes from the state and federal government. The federal government contributes $86 million, while $241 million comes from state government, including the general fund and the sales tax on motor vehicles. The Metropolitan Council gets 36 percent of the state motor vehicle sales tax. Thirty-nine percent of the Council's budget comes from transit fares and wastewater treatment charges. Ten percent of the budget is funded by a metropolitan-wide property tax and 4 percent is from other sources.

Tax-base Sharing in Metropolitan Minneapolis-St. Paul

The "Fiscal Disparities" program was begun in 1971 as a way of evening out the tax burden in the seven-county metropolitan area. The program shifts tens of millions of dollars a year among 240 local governments and school districts, and dozens of other taxing authorities in the metro area. Fiscal Disparities seeks to promote orderly economic development in the metro area, encourage protection of environmentally sensitive areas and ease financial pressures on lesser-developed communities.

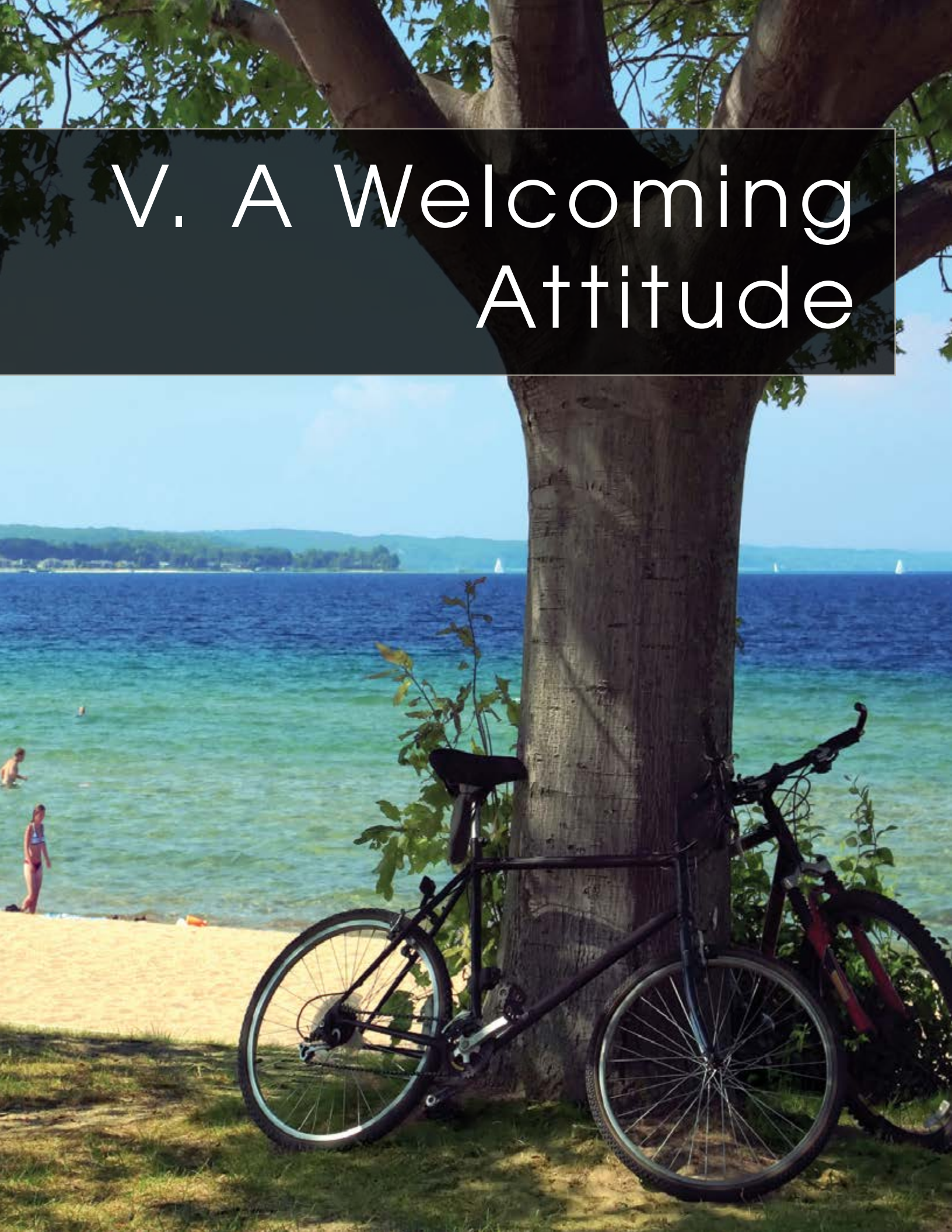
Under Fiscal Disparities, 40 percent of the growth in the commercial-industrial tax base since 1971 in the metro area goes into a shared pool, reducing the fiscal disparities among local units. Communities with a smaller per capita property value compared to the metro average get a larger distribution, while communities with a larger per capita property value get a smaller distribution.

Shared tax base totaled $390 million in 2013, or 37 percent of the total commercial-industrial tax base in the Twin Cities.

"Shared tax base totaled $390 million in 2013, or 37 percent of the total commercial-industrial tax base in the Twin Cities."

"In addition to long-range planning, the Metropolitan Council operates Metro Transit, which last year served 81 million bus and rail passengers, and operates the metro area's wastewater treatment system."

V. A Welcoming Attitude



Then-Minneapolis mayor R. T. Rybak grabbed national headlines last year when he embarked on a three-state tour to entice same-sex couples to get married in his city. Minnesota last year became the 13th state to legalize gay marriage and Rybak married 46 same-sex couples between midnight and 6:45 a.m. on Aug. 1, the day the law took effect. He then traveled to Illinois, Wisconsin and Colorado promoting his city as a destination-wedding site for same-sex couples. Rybak saw a big economic benefit in doing so.

A study by the Williams Institute at the University of California Los Angeles found Illinois could generate $103 million annually in new spending and $8.5 million in additional taxes if it were to legalize same-sex marriage. A bill that would have legalized same-sex marriage in Illinois failed to come to a vote before the legislature adjourned in June, but later was passed and signed into law.

In September, Rybak traveled to Chicago, where he said gay couples there should relocate to Minneapolis. "Ask yourself a question: If you were in a same-sex relationship and you wanted to start a business, would you rather start it in Chicago, where you are on your own, or come to Minneapolis where you can get married and that will give you rights to be on your partner's health insurance; so you can put that money into starting your business?" he said, according to the Chicago Tribune.

Over the years, Minnesota also has enacted a variety of welcoming initiatives. In May, the Legislature passed the "Dream Act," which makes undocumented students eligible for state grants, in-state college tuition and private scholarships. Students must attend a Minnesota high school for three years and either graduate or earn a GED.

Minnesota makes it easy to vote—easier than most states. Citizens must reside in the state only for 20 days in order to vote in an election. They also can register to vote on the date of an election by showing a driver's license or state identification card.

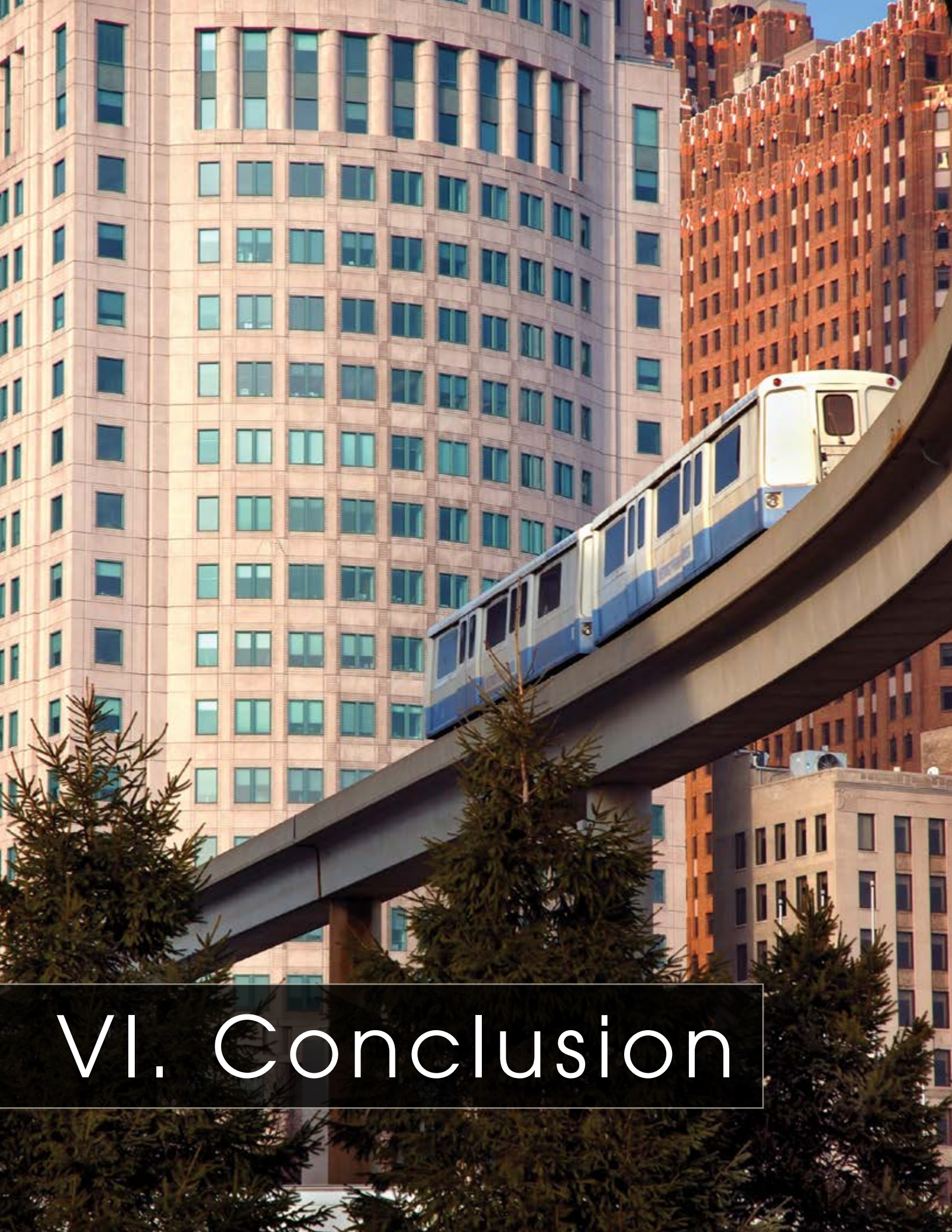
Minnesotans last year turned down a proposed constitutional amendment that would have required showing an ID before voting in future elections. And starting Aug. 12, 2014, Minnesotans will be able to obtain an absentee ballot without having to give a reason. Michigan has taken a much more restrictive stance in welcoming issues.

In 2004, voters passed a constitutional amendment that defines marriage as only between a man and a woman. The law is being challenged by two Hazel Park women in a same-sex relationship who cannot adopt each other's children under state law. That case is now being heard by a federal appeals court.

Unlike Minnesota, Michigan requires residents to present a valid picture ID when voting. The state does not have same-day voter registration. It requires residents to register to vote 30 days before an election. Michigan restricts absentee voting to those who are 60 years old or older, or cannot vote in person for a variety of reasons.

Michigan does not have a "Dream Act" like Minnesota, which allows undocumented students who graduated from state high schools to obtain in-state tuition, but several universities, including the University of Michigan and Wayne State University, have "Dream Act" policies. The U.S. Supreme Court recently upheld Michigan's 2006 constitutional ban on using race as a factor in university admission decisions. Minnesota does not have such a ban.

"Over the years, Minnesota also has enacted a variety of welcoming initiatives. In May, the Legislature passed the "Dream Act," which makes undocumented students eligible for state grants, in-state college tuition and private scholarships."



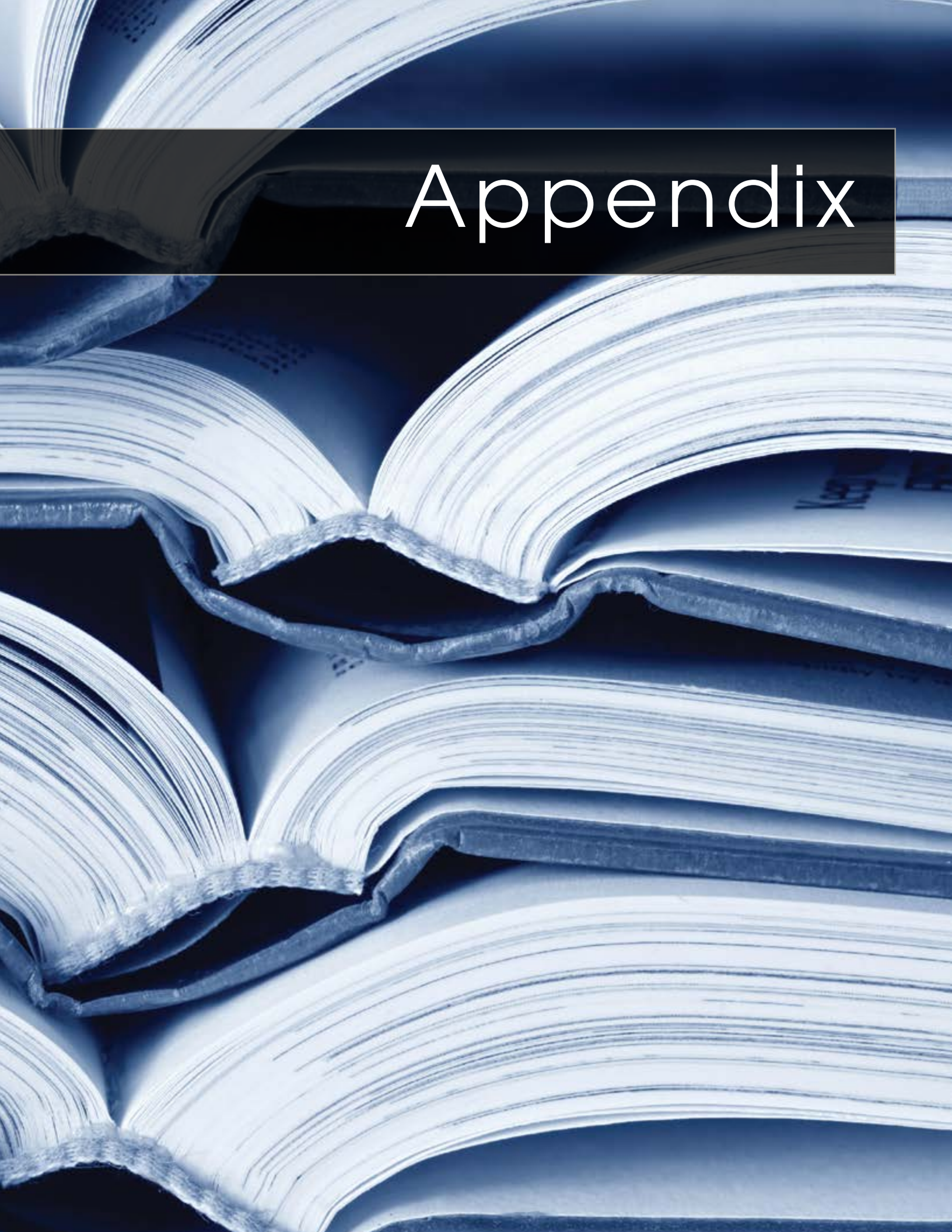
VI. Conclusion

Lawmakers and governors in many states, including Michigan, have focused primarily on cutting taxes and shrinking the size of their governments as the path to prosperous economies.

As this report has shown in detail, Minnesota has traveled a different path. There is no question Minnesota is a high tax state—as stated earlier, its residents paid $1,630 more than Michigan residents in state taxes alone last year.

But it has largely invested that additional revenue in services and investments that matter in a knowledge-based economy. An educated work force, efficient transportation systems, vibrant cities and metropolitan areas, and a secure safety net for those making the transition to a global economy all matter in creating a prosperous state.

Minnesota has made those necessary investments and enacted policies making the state welcoming to all. It really shouldn't be surprising, then, that it has the strongest economy in the Great Lakes region and one of the most vibrant in the country.



Appendix

Services Subject to Sales Tax in Minnesota

- Admission fees to exercise facilities and places of amusement
- Building cleaning and maintenance
- Delivery of aggregate material
- Detective and security services
- Fabrication labor
- Installation labor
- Laundry and cleaning services
  (Michigan levies its sales tax on industrial laundry services.)
- Lawn, garden-care, tree and bush services
- Massages that are not medically authorized
- Membership fees to sports and athletic facilities
- Motor vehicle towing, washing and rustproofing
- Parking services
- Pet grooming, boarding and care services
- Photography and video production
- Repair labor for businesses

Services Subject to Sales Tax in Michigan

- Telecommunications, wireless, and paging services
- Temporary accommodations (hotel, motel, lodges)
- Rental or lease of tangible personal property
  (rental cars, moving trucks, or leased automobiles)
- Laundry services for certain textiles
- Transmission and delivery of electricity if the electricity is not purchased for resale

Note: This report utilized data from numerous sources, including the Minnesota Department of Revenue, Minnesota Department of Management and Budget, Michigan House Fiscal Agency, Michigan Senate Fiscal Agency and Michigan Department of Management and Budget.

State Policies Matter:
How Minnesota's Tax, Spending and Social Policies Help it Achieve the Best Economy Among Great Lakes States

Report by: Rick Haglund

June 2014