

# LWVMI GOVERNMENT FINANCE STUDY

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Information for Local Leagues

August 2016



# Purpose of Study

Update current LWVMI position—Taxation and Budgeting



Three components of new study:

- Understand state revenue sources
- Examine state expenditures
- Look at state/local fiscal relationships

# LWVMI Taxation and Budgeting Position

## Parts of current position to be retained

- State-local tax structure: adequate, equitable, flexible, moderately progressive
- Rely on three broad based taxes—sales, income, property; rely more on income
  - Statewide use of scientific and uniform assessment methods and procedures; reappraise property exemptions periodically
  - State sales tax should exempt food and drugs
  - Graduated income tax rate
  - Other revenue sources: nuisance taxes, user fees
  - Endorse tax base sharing

## Taxation and Budgeting Position (cont.)

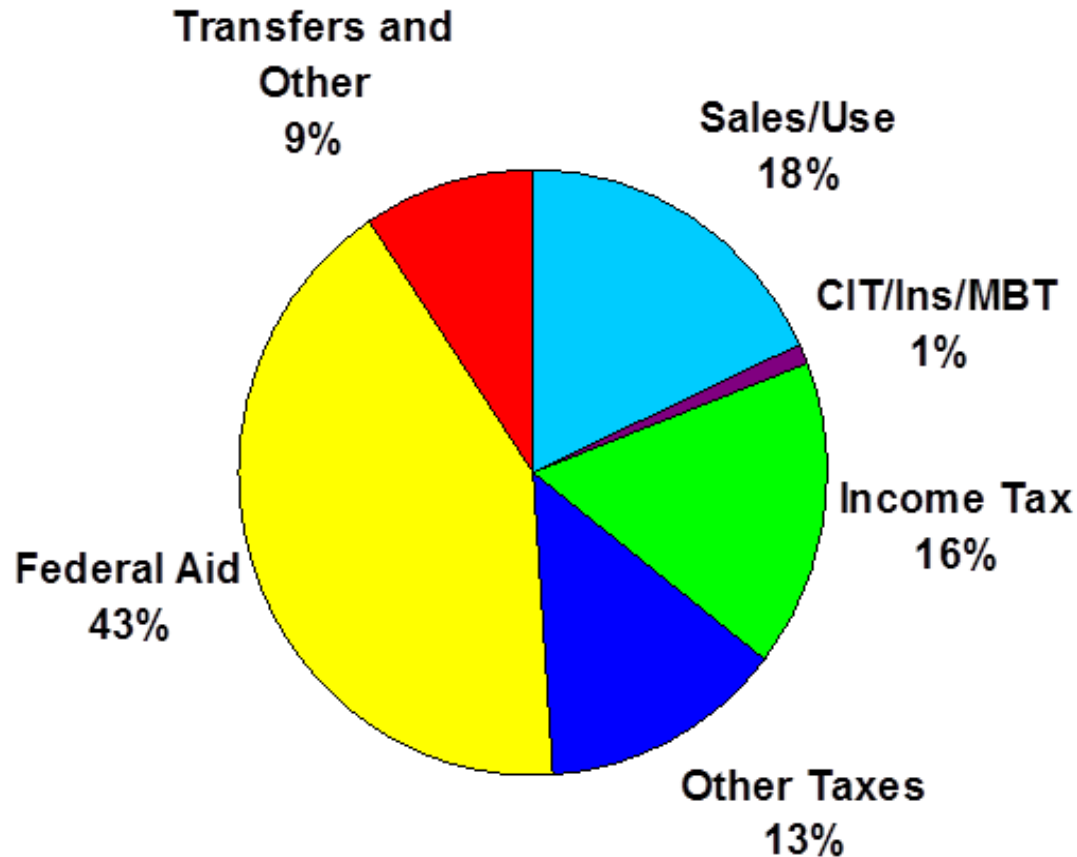
- Broad, fundamental taxing powers for legislature
- Legislature should delegate to local units alternatives to property tax
- State-collected revenues should be distributed on basis of need, minimum level of local support, and cost of needed services

# Michigan's \$53.7 Billion Budget

- Funds state programs and services; adopted annually by legislature, signed by governor
- Must be balanced each year
- Three major sources of revenue:
  - Sales tax
  - Income tax
  - Federal funds
- Three divisions of total:
  - General Fund
  - State School Aid Fund
  - Restricted monies

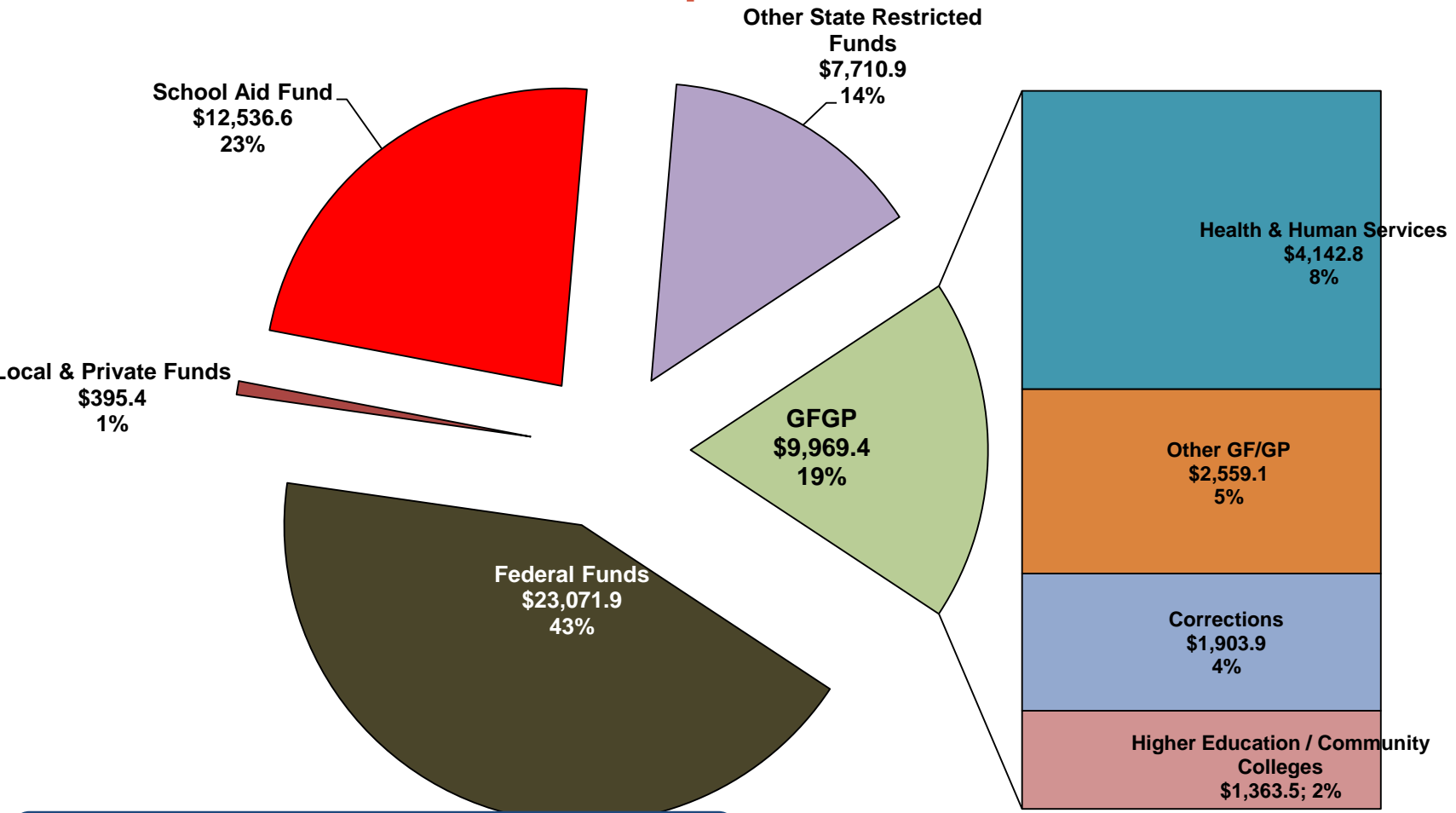


# Michigan's Major Revenue Sources



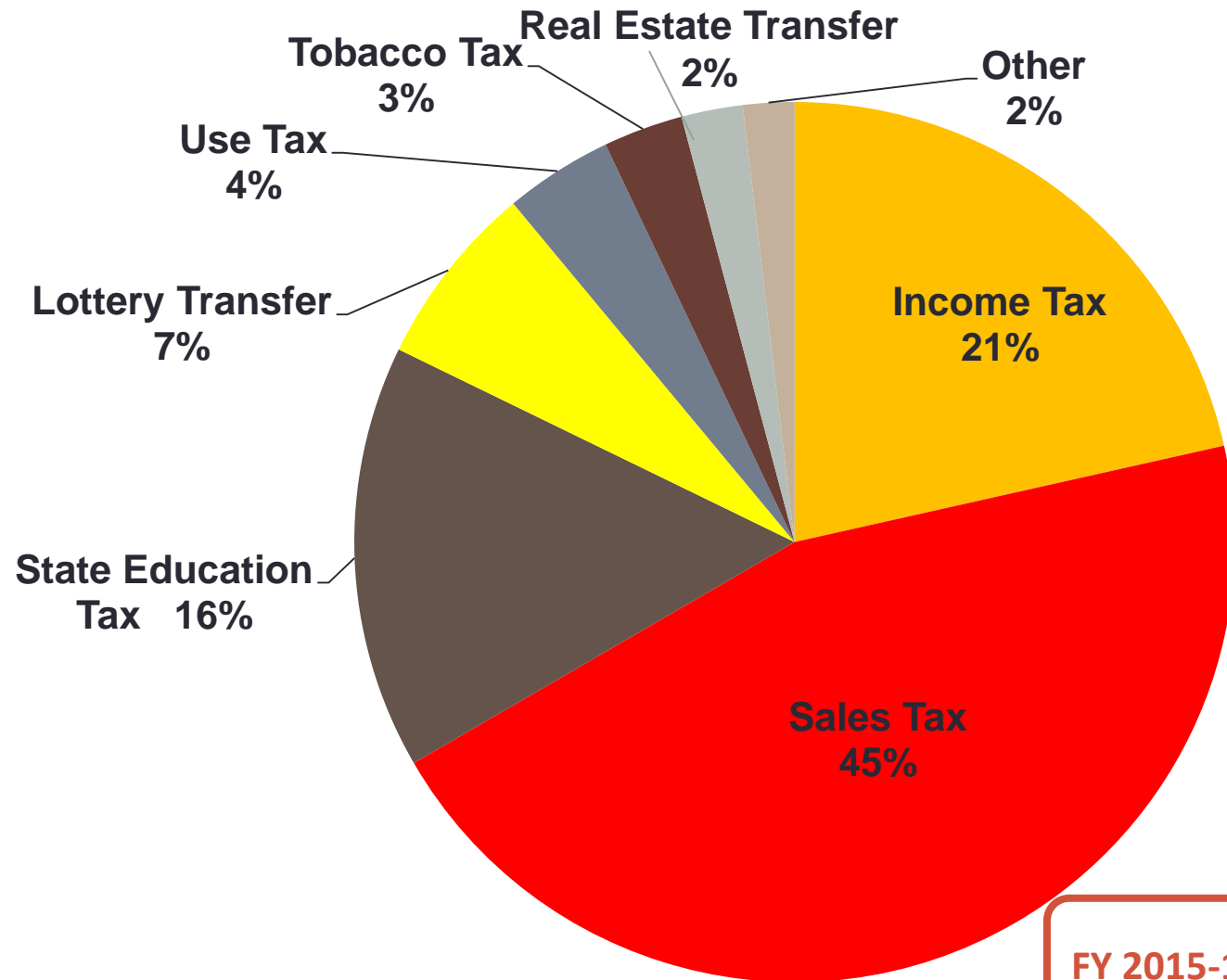
**FY 2016 Total Revenue Estimated at \$53.7 Billion**

# General Fund Expenditures as % of Total



**Total State Budget of \$53,700 Million**

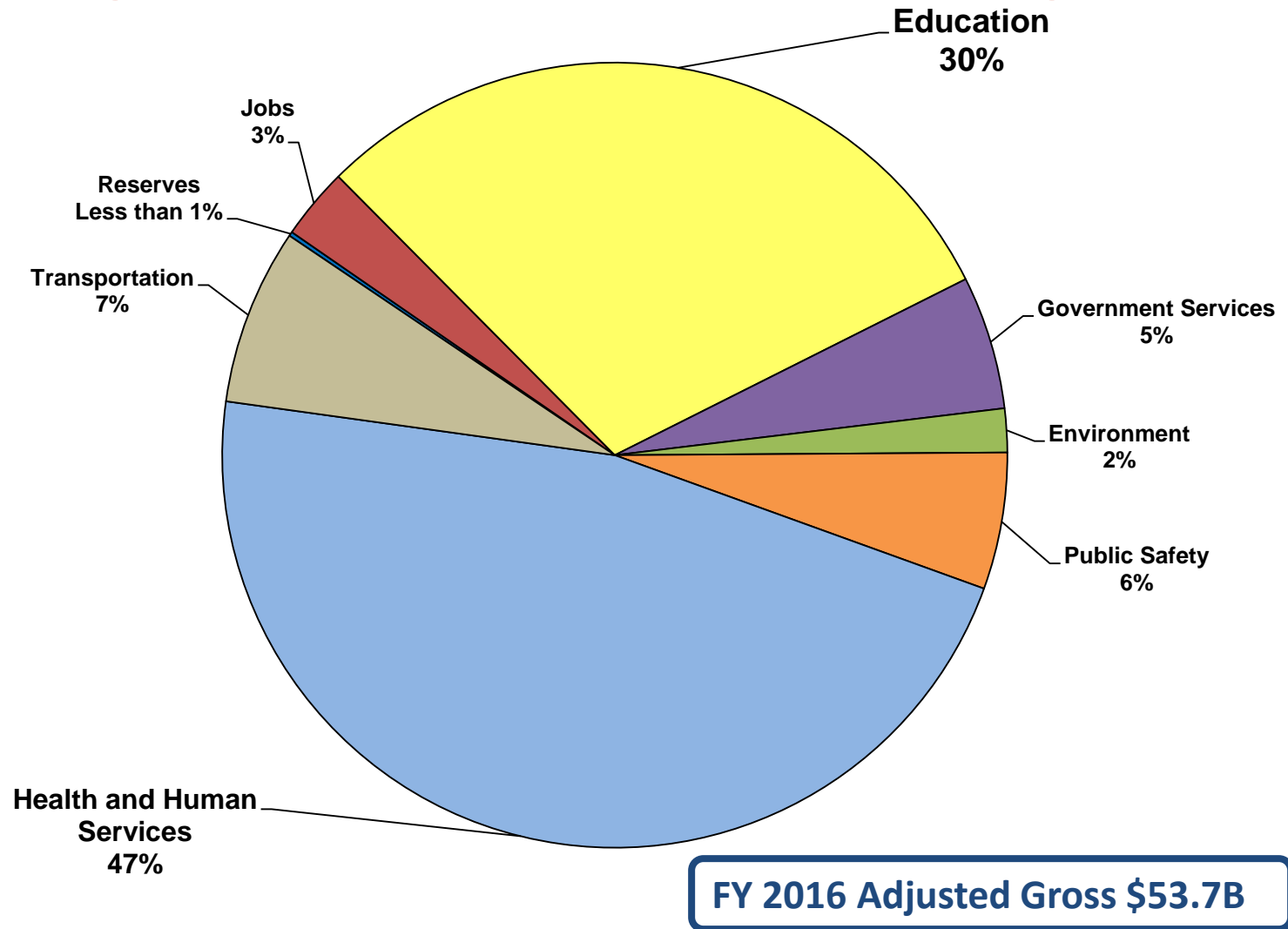
# School Aid Fund Revenue Sources



FY 2015-16 Total of \$12.1 Billion



# Michigan's Current State Budget



# Changes in State Funding FY 2001 – FY 2015

<b>Program</b>	<b>% Change</b>	<b>% Change Adjusted for Inflation</b>
Health & Human Services	16.1%	10.7%
Corrections	21.0%	- 9.8%
Revenue Sharing	-21.0%	-41.1%
Higher Education	-31.0%	- 48.5%
School Aid Fund	10.6%	-17.6%
Federal Aid	101.4%	50.0%

# Recent Changes in State Tax Policies

- Eliminated many personal income tax deductions
- Instituted tax on pensions
- Reduced corporate income tax
- Eliminated personal property tax on businesses
- Increased transportation taxes, fees; earmarked future General Fund monies for transportation

# Tax Relief for Low-Income and Seniors

## Homestead Property Tax Credit

- For seniors and veterans; tax credits on rental property; home heating credit

## Earned Income Tax Credit

- For working families, individuals.



# Sales Tax

- 6% rate; constitutional amendment needed to change rate
- Legislature can expand base to include services
- A tax on services could generate more revenue, reflecting the growing service economy.
- Only 4 states tax most of the 164 potential service categories.
- Michigan and many other states have tried unsuccessfully to tax services

# “Nuisance Taxes”

## Tax

## Last increase

- Tobacco products 2004
- Liquor mark-up 1983
- Beer, wine, mixed spirits 1980



# Business Taxes

- Michigan's Corporate Income Tax--2011
  - 6% on corporate income
  - 1.25% on insurance premiums
  - 0.29% franchise tax on financial institutions
- Applies to entities doing business in Michigan--gross receipts more than \$350,000
- Net business taxes were 15% of total state revenue in 1991; 4.8% in 2013; 1% in 2015

# Federal Funds

- Federal funds make up 43% of the total revenue
- Designated for specific purposes by state or federal law or by state constitution for education, transportation, Medicaid, etc.



# Fees, fines, permits

- Increasingly important revenue source for state, local governments
- Can disproportionately impact low-income residents
- Michigan Supreme Court (1998, Bot v. City of Lansing)--criteria for fee vs. tax
  - Must serve a regulatory purpose, not revenue-raising
  - Must be proportionate to necessary cost of services or commodity; imposed on those benefitting
  - Voluntary

# Transportation Funding

## Per Capita Highway Expenditures, 2013

<b>State</b>	<b>Expend Per Capita</b>	<b>Rank</b>
<b>Pennsylvania</b>	<b>\$558</b>	<b>19</b>
<b>Wisconsin</b>	<b>\$535</b>	<b>23</b>
<b>Minnesota</b>	<b>\$524</b>	<b>25</b>
<b>Ohio</b>	<b>\$512</b>	<b>26</b>
<b>Illinois</b>	<b>\$443</b>	<b>37</b>
<b>New York</b>	<b>\$432</b>	<b>39</b>
<b>Indiana</b>	<b>\$430</b>	<b>40</b>
<b>Michigan</b>	<b>\$305</b>	<b>50</b>
<b>United States</b>	<b>\$584</b>	

# 2015 Road Funding Law

- **Jan. 2017**--Taxes on gasoline, diesel fuel— up from 15 and 19 cents to 26.3 cents
- **2017**--Registration fees up by 20%--higher fees for heavier vehicles, plug-ins and hybrids
- **2017**--Expand Homestead Property Tax Credit to offset higher transportation taxes.
- **2018**--Portion of state income tax revenue earmarked for Michigan Transportation Fund
- **2022**--Gasoline and diesel fuel taxes indexed to inflation

# State Budget Process

- Early Feb.
- Governor's budget introduced
- .
- Budget bills sent to appropriations subcommittees in both houses
- Apr.-May
- After approval in one house, bills move to other house—same process

# Budget Process—cont.

- Late May
  - Budget targets agreed to; bills pass 2<sup>nd</sup> house
- Early June
  - Bills sent to conference committee
- Late June
  - Final budget passage; Gov. signs—can line-item veto
- October 1
  - Beginning of new fiscal year

# Concerns--State Budget Process

- Legislative committees playing less of an oversight role
- Governor's budget: less detailed; departmental budgets grouped together
- Diminished role of citizens' committees
- Fewer opportunities for public comment
- Adding an appropriation to controversial legislation—can't be subject to a referendum

# Tax expenditures

- Includes tax exemptions, credits, deductions, exclusions, deferrals, preferential taxes
- \$14 billion in FY2000, \$27 billion in FY2016
- Can benefit targeted taxpayers
- Difficult to quantify or eliminate

# Issues Facing Local Governments

- 1,773 units of Michigan local government— vary greatly in size, service delivery
- Primary revenue source—**property tax**. Taxable value of property varies greatly.
- Limited options for locals to raise revenue.
- Tax limitations (Headlee, etc.)
- State statutory revenue sharing--vulnerable to economic cycles and legislative priorities.

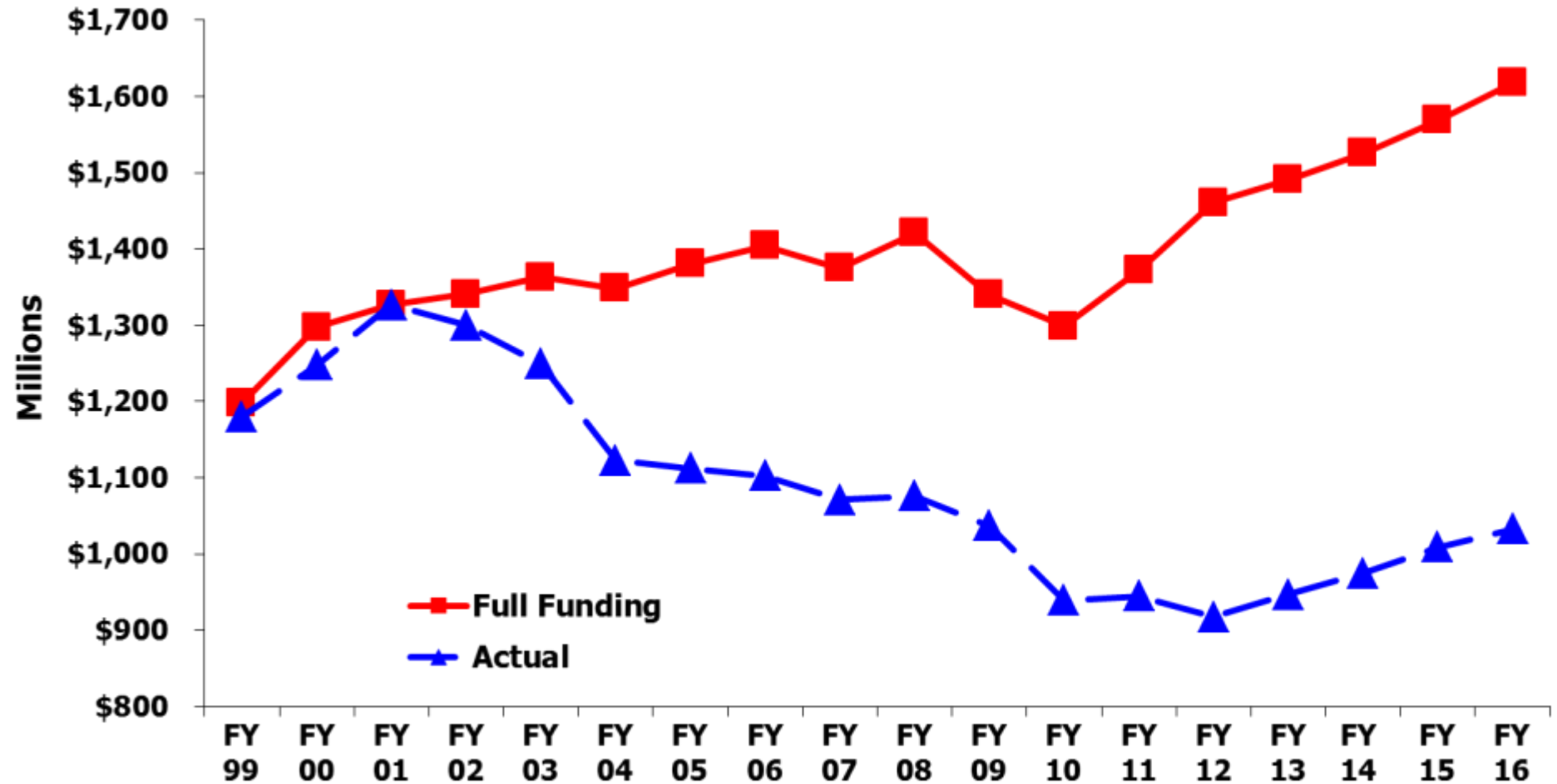


# State Revenue Sharing

Two types:

- **Constitutional:** 15% of sales tax (4% rate) goes to cities, villages, townships (CVTs). Remaining 2% sales tax rate goes to State School Aid Fund.
- **Statutory:** Distributed by law, paid to eligible CVTs and counties. Money comes from 21.3% of 4% rate of sales tax.

# Total Revenue Sharing Payments to Cities, Villages, and Townships



# Property Taxes and Local Governments

- Primary revenue source for cities, townships, villages, counties
- Other sources: state and federal governments, fees and fines, local taxes
- Constitutional limitations on property tax (Headlee, tax allocation)
- Numerous credits and exemptions for certain property taxpayers; also to encourage economic development

# LWVMI Government Finance Study Committee Members

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