Michigan League FOR Human Services
CELEBRATING 100 YEARS OF RESEARCH AND ADVOCACY

Revised
April 2012

Replacing Revenue Key to Successful Personal Property Tax Overhaul

More Cuts, Another Tax Shift to Individuals, Not the Answer

by **Joanne Bump**
Senior Policy Analyst

Issue

Following months of speculation about a proposal to reduce or eliminate the Personal Property Tax, Senate Bills 1065–1072 were introduced April 17, 2012, to dramatically reduce the PPT. The Personal Property Tax is a tax paid by businesses on property not attached to a structure, such as business machinery, equipment and tools. It provides significant revenue to local governments, schools and community colleges. The PPT is a widely accepted tax as 43 states have some tax on personal property.[1] If the PPT is reduced, it is vital that replacement revenue be found from businesses — rather than individual taxpayers who are already paying a disproportionate share — to maintain local fire, police and other services.

The Proposal

The Senate package would set a threshold where businesses with industrial or commercial personal property valued at less than $40,000 would be exempt from the tax. This change, by itself, fully exempts the majority of all commercial and industrial parcels. In addition, it phases out the remaining tax on industrial personal property beginning in 2016 by exempting new manufacturing personal property and phasing out existing manufacturing personal property over seven years. Expiring business tax credits are used to replace some of the lost revenue that the Personal Property Tax generates and establishes a reimbursement mechanism to locals.

The suggested replacement revenue source is the phaseout of the certified credits that have been honored after the Michigan Business Tax was ended. While these credits have a limited life, the phaseout schedule needs to match the new revenue stream. The revenue is lower than the amount needed for full replacement and only a small portion will become available by FY 2016. Given this timing, MBT credits are not likely to provide enough funds for immediate replacement revenue as shown in the table.

Michigan Certified Business Credits
Estimated Revenue for Credits Claimed
(in millions)

Fiscal Year	Credits Claimed	Annual Change	Replacement Revenue Available	Estimated Revenue Loss
2012	$282	—	—	—
2013	$502	$220	—	($80)
2014	$624	$122	—	($80)
2015	$623	($1)	—	($81)
2016	$502	($121)	$122	($454)
2017	$367	($135)	$257	($481)
2018	$353	($14)	$271	($506)
2019	$344	($9)	$280	na

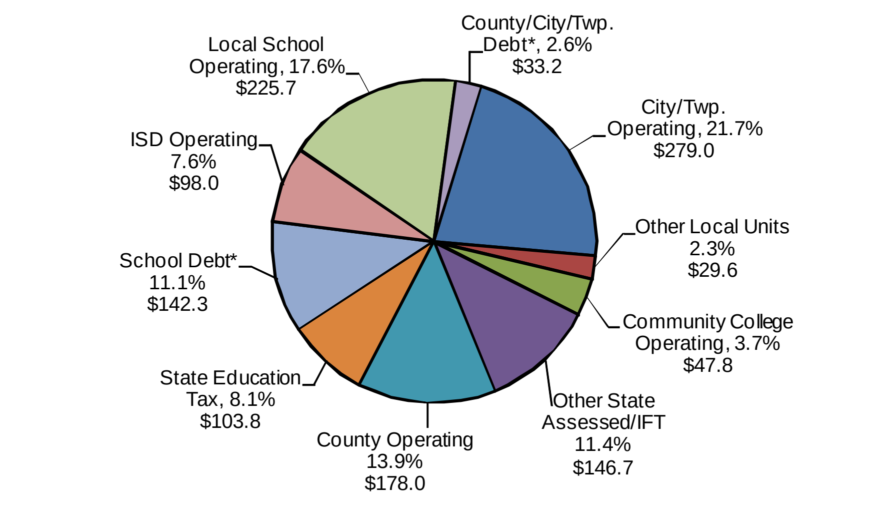
Source of Credits Claimed: Department of Treasury as reported by Bridge, April 2012.
Source of Revenue Loss: Senate Fiscal Agency, April 19, 2012.
Table prepared by Michigan League for Human Services.

[1] National Council of State Legislatures comparison, March 2011.

Current Tax and Impact on Local Governments and Schools

Personal Property Taxes by Source of Levy, 2010

(in millions)



*Note: The majority of this debt is city/township, or local school debt, respectively.

Source: Senate Fiscal Agency

About $1.2 billion in revenue from the industrial, commercial and utility PPT is collected annually. This revenue goes to counties, cities, townships, villages, local and intermediate schools, and community colleges. The largest portion of the PPT provides operating revenue for cities, counties and townships. According to the Senate Fiscal Agency, these local units received an estimated $457 million from the PPT in 2010 — about 35% of all PPT paid in Michigan. Local schools received about $226 million for operations in 2010 and an additional $99 million for debt payments. Additional PPT revenue goes to Intermediate School Districts and community colleges.

While it varies, the percent of a local government, school or community college budget that relies on the Personal Property Tax can be very sizable. The Michigan Association of Counties reports that the amount of PPT collected as a percentage of each county's total budget for 2010 ranges from 2% to more than 27%. For the revenue impact on individual communities and schools, see the Senate Fiscal Agency's report, *The State and Local Impact of Property Taxes Levied on Michigan Personal Property Taxes*.

Because of the significant potential impact on local government and school revenues, a number of the local government and school associations have called for a constitutional guarantee that revenues lost from a change to the PPT be replaced for local communities and schools. They have argued that without such a guarantee, local revenues could be lost or diverted, resulting in a reduction of services. This is of particular concern given that the Michigan Municipal League reports that revenue sharing has been cut over $5 billion in the last decade.

Impact on Businesses and Individuals

The proposed $1.2 billion tax cut for businesses through the elimination of the PPT follows tax changes in 2011 that cut state business taxes by 83%, or $1.6 billion. This means two-thirds of Michigan businesses do not pay any state income tax.

The business tax cut in 2011 was paid for by increasing taxes on individual taxpayers by 23%, or $1.4 billion, in FY 13. As a result, 51% of Michigan residents will pay more personal income tax after FY 12. In addition, the lowest-income families were the hardest hit by the income tax changes; they will pay 1% more in taxes as a percent of their income, or $101 more. The highest-income group will pay an average of 0.001%, or $7, more per year.

Individual taxpayers, who are already paying more as a result of the 2011 tax changes, may again bear the brunt if PPT revenues are not replaced. According to those advocating for guaranteed replacement revenues, eliminating all, or in some cases a portion, of the PPT funds would trigger automatic millage increases on homeowners in school districts still legally obligated to repay bonds but without the PPT funds to do so. Policymakers have suggested raising the sales tax for replacement revenue. It may provide revenue, but again it shifts taxes to individuals and makes Michigan's tax structure even more regressive.

Public Support for PPT

In April, an EPIC-MRA poll showed that 70% of Michigan voters oppose eliminating or significantly cutting the Personal Property Tax when those polled were told that the PPT pays for local services such as police and fire protection and schools. Opposition to eliminating or significantly cutting the PPT increased to 78% when those polled were told that cuts to local services would likely result. The poll also showed that 58% would support a constitutional amendment to require the Legislature to fully replace all of the revenues and to guarantee the funds continue to go to local communities and local schools.

Policy Recommendation

The elimination of personal property taxes will put at risk local services that need to be maintained, not reduced. Full revenue replacement from any change to the Personal Property Tax is vital. In addition, businesses need to continue to pay taxes that support services they use such as police and fire services for their buildings. The Corporate Income Tax could be used as a mechanism to provide replacement revenue by raising the rate or expanding the base.

Replacement revenue plans should not rely on cutting local services or shifting taxes onto individuals who will already be paying more. Instead, businesses should continue paying the same amount of revenue as before the proposed Personal Property Tax reduction.