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NEW STATE REVENUE SHARING FORMULA

Senate Bill 259 with House Committee amendments
First Analysis (6-17-87)

Sponsor: Sen. Harry Gast
Senate Committee: Finance
First House Committee: Taxation
Second House Committee: Appropriations

THE APPARENT PROBLEM:

Under the State Revenue Sharing Act, the state shares revenues from state personal income and single business taxes with cities, villages, townships, and counties based on a formula which measures a local unit's "tax effort" (calculated by dividing the local unit's property, local income, and excise taxes by its state equalized valuation) and compares that to the statewide average. The higher a unit's local tax effort is, the more it will receive from the state in shared revenue payments.

Although the 1971 state revenue sharing law does not permit the inclusion of special assessments in the revenue sharing formula, until 1984 some local units of government had been improperly including certain special assessments (primarily those for police and fire protection) in their reports of local tax rates to the Department of Treasury. In October, 1983, a study by a citizen's group noted this fact, and the following year the treasury department revised its reporting forms to require local units of government to identify clearly each tax or assessment they levied.

Since the total amount of revenue sharing money remains fixed, the change in reporting requirements meant that a shift in revenue sharing payments occurred, with payments to some local units — mainly large cities — increasing while payments to other units — mainly townships — decreased. In addition, since revenue shared with the state represents anywhere from 15 percent (for some cities) to 40 percent (for small townships) of the operating funds of local governments, this shift in revenue sharing posed potentially serious financial problems for those townships and smaller cities whose payments would be significantly reduced if special assessments were no longer included in the calculation of their local tax effort. In 1985, the legislature voted to appropriate money from the state general fund to make up the losses suffered by townships and smaller cities due to the new reporting requirements. However, no such supplemental payment was voted for subsequent fiscal years, and those units experiencing reduced revenue sharing payments are faced with a total potential loss of nearly $2.5 million.

Some people believe that this change has placed an unfair burden on some townships and smaller cities, and requested legislation that includes certain special assessments in the determination of a local unit's tax effort, thereby restoring lost revenue sharing money to these local governments. As passed by the Senate, Senate Bill 40 would have included special assessments as part of a local unit's tax effort. However, since restoring the $2.5 million to townships would result in larger cities losing the same amount, the House passed a version of Senate Bill 40 that would "hold harmless" all units of government by requiring the legislature to make annual appropriations of up to $2.5 million to ensure that no local unit of government lost shared revenue under the bill. The two different versions of Senate Bill 40 passed by the House and the Senate are now in conference committee. A compromise solution to the problems generated by including special assessments in calculating the relative tax effort has been proposed in conjunction with the solutions proposed in Senate Bill 40.

THE CONTENT OF THE BILL:

The bill would amend the Income Tax Act, by changing formulas in the act, to increase the amount of income tax revenue allocated to state revenue sharing payments for distribution to local units of government. Under the bill, payments to cities, villages, and townships would increase, while payments to counties would remain unchanged.

Section 481 of the Income Tax Act, which would be amended by the bill, currently provides that 12.1 percent of the gross income tax revenues (before refunds) is shared with local units of government. That percentage is in the same ratio as 2.6 percent bears to the average income tax collection for the quarter preceding the quarter in which the income tax revenues are distributed to the local units. The bill would change the percentage distribution of income tax revenue from 12.1 percent of 2.6 percent (the income tax rate at the time the bill was written) to 6.91 percent of 4.6 percent (the current income tax rate).

Current law gives 35 percent of the shared revenue to counties on a per capita basis and 65 percent to cities, villages, and townships on a relative tax effort (RTE) basis. The bill would change these percentages to 34.65 percent and 65.35 percent respectively. This will result in counties receiving the same amount in fiscal year 1988 as they would otherwise have received, with the increase going to cities, villages, and townships.

The bill is tie-barred to Senate Bill 40, which addresses the inclusion of certain special assessments in calculating revenue sharing and which currently is in conference committee.

MCL 206.481

HOUSE COMMITTEE ACTION

As passed by the Senate, the bill specified that 6.896 percent of the gross income tax collections before refunds would be allocated to state revenue sharing, with 34.7 percent of the revenue sharing going to counties and 65.3 percent going to cities, villages, and townships. The House Appropriations committee changed these percentages to 6.91, 34.65, and 65.35 respectively.

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that the change in percentage distribution would shift between $2.5 million and $2.8 million from the state general fund to state revenue sharing monies. (6-10-87)

ARGUMENTS:

OVER

For:

The bill, in conjunction with Senate Bill 40, would ensure that no local governmental unit would have its revenue sharing payments reduced as a result of including certain special assessments in the calculation of a local unit's tax effort rate. In addition, the bill would eliminate the need, which exists under Senate Bill 40 (as passed by the House of Representatives), for the legislature to appropriate additional money from the general fund every year in order to "hold harmless" all local units of government.

Against:

While the bill would allow a formula under Senate Bill 40 which would keep all local units "whole" when altering the language dealing with the relative tax effort formula in fiscal year 1988, by itself it only adds the $2.5-$2.8 million to revenue sharing. This amount may not be enough to keep all government units whole under Senate Bill 40 in subsequent fiscal years, since this will depend upon the taxing behavior of the local units in future years and on the formula chosen in Senate Bill 40.

Against:

The bill would result in a reduction of state general funds of $2.5-$2.8 million in fiscal year 1988. The solution to the relative tax effort formula should be resolved within the existing funds already available for revenue sharing, and not by "raiding" the general fund.

POSITIONS:

The Michigan Municipal League supports the bil. (6-16-87)

The Michigan Townships Association supports the bill. (6-16-87)