SFA BILL ANALYSIS

Senate Fiscal Agency • Lansing, Michigan 48909 • (517) 373-5383

Senate Bill 704 (Substitute S-7 as reported)
Senate Bill 854 (Substitute S-2 as reported)
Senate Bill 896 (Substitute S-2 as reported)
Sponsor: Senator Norman D. Shinkle (S.B. 704)
Senator Gilbert J. DiNello (S.B. 854)
Senator Richard D. Fessler (S.B. 896)
Committee: Finance

Date Completed: 9-10-90

RATIONALE

Michigan's property tax system and the burden that it places on the taxpayers have long been the target of considerable complaint; the tax has been called the State's most onerous by some, an impediment to business and economic development by others. Traditionally, Michigan property taxes have ranked among the highest when compared to property tax levels in other states. This has spawned a debate that has been lengthy and continuing. In an attempted response to the problems, there have been both legislative and citizen-initiated proposals, some of them considered drastic, to alter the State's property tax system and the local government and school financing system. Three proposals were placed on the 1978 ballot and three were placed on the 1980 ballot to revise, most notably through property tax reform, the State's tax structure. All were defeated except the Tax Limitation Amendment (Proposal E, or the Headlee Amendment) in 1978. After those defeats, the emphasis in the battle over tax policy switched to the income tax, which was raised and lowered twice from 1982 to 1986. Though the property tax issue did not seem as urgent in the mid-1980s as it had earlier, it did not go away, and it reappeared on the ballot in 1989 in Proposal B. Proposal B, if passed, would have made substantial changes to the property tax system, but would have replaced the reduced revenue by increasing the sales tax by 2 cents. The Proposal was defeated by a wide margin.

Some people have taken the sound defeat of Proposal B, coupled with continuing calls for property tax relief, to mean that taxpayers want property taxes reduced, not shifted to another type of tax. Add to this the recent widespread complaints of substantial increases in property assessments across the State, and the fact that five separate groups notified the Secretary of State's Office that they were circulating petitions to place on this year's ballot language to alter the property tax system, and it can be seen that concerns about high property taxes are increasing once again. In both his State of the State Message and budget message, the Governor proposed reducing the burden of local school property taxes on homeowners by limiting future assessment increases to the rate of inflation.

In response to these suggestions and the public outcry, the House passed a three-bill package in early March that not only would limit assessment increases on a taxpayer's homestead to the rate of inflation, but also would expand the homestead property tax credit, and eliminate the capital acquisition deduction under the Single Business Tax Act. The Senate then passed an eight-bill package to reduce property assessments and index assessment increases to the rate of inflation, exempt seniors and handicappers from paying school operating millages, and expand the homestead property tax credit. Neither package has advanced past its first house; the House package has been criticized as providing little or no real tax relief, and the Senate version has been criticized as being too expensive. It has been suggested as an alternative that a proposal simply to cap assessment increases may be preferable to the previous approaches.

CONTENT

Senate Bill 704 (S-7) and Senate Bill 854 (S-2) would amend the Single Business Tax Act and the Income Tax Act, respectively, to allow a taxpayer to claim a tax credit against property assessment increases that exceeded the rate of inflation. Senate Bill 896 (S-2) would amend the General Property Tax Act to revise requirements pertaining to assessment notices. The three bills are tie-barred to each other.

Senate Bill 854 (S-2)

The bill would amend the Income Tax Act to allow a taxpayer to calculate and claim a credit against the income tax equal to the amount by which the State equalized valuation (SEV) used to calculate school taxes on his or her property exceeded inflation, or 5%, whichever was less. (For a detailed description of the calculation, see below.) Any SEV increases attributable to new construction or improvements on a property could not be included as part of the SEV increase on the property for purposes of calculating the credit.

The credit would be a refundable credit (that is, it could exceed a person's tax liability). The bill provides that the amount of property taxes used by a taxpayer to calculate his or her homestead property tax credit would have to be reduced by the amount of the credit claimed under the bill. If a person had an unpaid tax liability, the State Treasurer would have to apply any credit claimed under the bill against the unpaid liability before disbursing the credit.

To receive the credit, a taxpayer would have to attach to his or her income tax return the property tax bill for the property for the tax year for which the return was filed, the property tax bill for the prior year, and any assessment change notice for the property.

To calculate the credit a taxpayer would have to do the following:

-- Divide the SEV of the property (in the tax year for which the return was filed) minus the amount of SEV attributable to new construction and improvements for that year, by the prior year SEV to produce "A".
-- Subtract from A the inflation rate (for the tax year immediately preceding the tax year for which the return was filed) or 5%, whichever was less, to produce "B".
-- Multiply B by the property's prior year SEV to produce "C".
-- Multiply C by the school operating tax (for the year in which the return was filed) to produce "D".
-- Add to D the amount of the credit claimed by the taxpayer for the property in the preceding tax year, to produce the credit.

The bill would apply to tax years beginning after 1990.

Proposed MCL 206.280 and 206.281

Senate Bill 704 (S-7)

The bill would amend the Single Business Tax Act to allow a taxpayer to calculate and claim a credit against the SBT equal to the amount by which the SEV used to calculate school taxes on his or her property exceeded inflation, or 5%, whichever was less. (For a detailed description of the calculation, see below.) Any SEV increases attributable to new construction or improvements on a property could not be included as part of the SEV increase on the property for purposes of calculating the credit.

The credit would be a refundable credit (that is, it could exceed a person's tax liability). If a person had an unpaid tax liability, the State Treasurer would have to apply any credit claimed under the bill against the unpaid liability before disbursing the credit.

To receive the credit, a taxpayer would have to attach to his or her SBT return the property tax bill for the property for the tax year for which the return was filed, the property tax bill for the prior year, and any assessment change notice for the property.

A person could not claim a credit under the SBT Act for any property for which a credit was claimed for the same year under the Income Tax Act.

To calculate the credit a taxpayer would have to do the following:

- -- Divide the SEV of the property (in the tax year for which the return was filed) minus the amount of SEV attributable to new construction and improvements for that year, by the prior year SEV to produce "A".
- -- Subtract from A the inflation rate (for the tax year immediately preceding the tax year for which the return was filed) or 5%, whichever was less, to produce "B".
- -- Multiply B by the property's prior year SEV to produce "C".
- -- Multiply C by the school operating tax (for the year in which the return was filed) to produce "D".
- -- Add to D the amount of the credit claimed by the taxpayer for the property in the preceding tax year, to produce the credit.

The bill would apply to tax years beginning after 1990.

Proposed MCL 206.34

Senate Bill 896 (S-2)

The bill would amend the General Property Tax Act to provide that an assessment notice would have to be sent to a property owner if there were an increase or decrease in an assessment. Currently, assessors must send each property owner on an assessment roll notice of an increase in an assessment.

The Act requires an assessment notice to contain various information about the property being assessed, such as its classification and its SEV from the previous year. The bill would require that an assessment notice also include the amount of the assessment attributable to new construction and improvements.

MCL 211.24c

FISCAL IMPACT

It is not possible to provide a precise estimate of the reduction in property taxes due to the SEV tax credit provided by the bills. The tax reduction would depend on annual inflation rates and growth in SEV, and the distribution of SEV growth among and within school districts. In the first year, net tax credits probably would be increased by $70 million to $80 million, and would rise in each year thereafter in which SEV outpaced inflation. For further information see Senate Fiscal Agency Memorandum of 9-5-90.

ARGUMENTS

Supporting Argument

Periodically, over the last 15 years, dissatisfaction with the property tax system has peaked, and each time efforts have been made to find better ways to raise and distribute tax dollars for those units that rely on them the most: the schools and local governments. Time and again, attempts at creating lasting reform have been frustrated by the enormous complexity of the task and by the competing and conflicting goals of the parties involved. In 1989, the latest attempt to address the problems of property taxes, school finances, and local government finances, saw the placement of two proposals on the ballot. The voters soundly rejected both Proposal A (to increase school funding by increasing the sales tax by 1/2 cent) and Proposal B (to raise the sales tax by 2 cents, and dedicate 1-1/2 cents to property tax relief and 1/2 cent to school funding). From 1978 on, voters have been confronted with, and (except for the Headlee Amendment) have rejected various ballot proposals that would have slashed property taxes drastically in an effort to reduce the size and influence of government, and others that would have shifted reliance on the property tax to either the sales or the income tax. Repeated attempts in the Legislature to resolve the issues also have failed.

Though ballot proposals and legislation have come and gone, high property taxation is an issue that has not gone away. One common theme remains: the people want property tax relief. The bills would cause a substantial and lasting reduction in the amount of property taxes that taxpayers pay, and thus at long last would provide real property tax relief.

Supporting Argument

It is time for the State to stop talking about lowering property taxes and adopt some meaningful relief. Year after year property tax reduction proposals are put forward yet never become law, resulting in increased property taxes. One of the main problems is continually increasing assessments. The State Treasurer reports that in the past three years assessments on residential property have increased by 19% while inflation has increased 9%. It has been reported that commercial property assessments in Detroit have increased an average of 23%, this year. This is an example of a tax system gone haywire, and in immediate need of repair. The bills would address this problem directly by allowing a taxpayer to claim an income tax credit (or SBT credit) that would, in effect, limit the taxpayer's property tax assessment in a year to the rate of inflation or 5%, whichever was less. This would effectively mean that the only school tax increases homeowners saw would be those they voted for.

Response: While the bills would limit increases in assessments, it must be remembered that assessments reflect the value of a property. Property is required to be assessed at 50% of true cash value, and thus an assessment is generally established at a level of 50% of the average selling price in an area. A dramatic rise in property taxes in some areas is not so much a reflection of a property tax system out of control as it is simply a rise in property values. When properties in an area sell for amounts greater than their current assessed level of value, assessments for the following year probably will rise. Since property values in the State, especially in some areas, have been rising in the past few years, it is no surprise that assessments also have been rising. Another reason for an individual property assessment's taking a dramatic increase can be quite simple. Assessors' staffs do not usually have the resources to visit and evaluate individual properties on a regular basis. If a property has not been visited in 20 years, and the owner or owners of the property have made substantial improvements, the property likely will experience a substantial assessment increase the next time it is inspected or sold. While it may be unpleasant for the property owner to cope with a sudden increase in his or her property tax bill, an argument can be made that the property may have been under-assessed for several years.

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