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10/20 HOMEOWNER TAX CREDIT PLAN

House Bill 4613 (Substitute H-1)
Sponsor: Rep. Teola Hunter

House Bill 4605 as introduced
Sponsor: Rep. Debbie Stabenow

House Bill 4606 (Substitute H-1)
Sponsor: Rep. H. Lynn Jondahl

House Bills 4607 and 4609 as introduced
Sponsor: Rep. Bob Emerson

House Bill 4608 and 4612 as introduced
Sponsor: Rep. Mary C. Brown

House Bill 4610 as introduced
Sponsor: Rep. Perry Bullard

First Analysis (6-23-87)
Committee: Taxation

THE APPARENT PROBLEM:

Governor Blanchard has proposed a property tax cut plan that would return $200 million every year to over two million Michigan households. The plan is called the 10/20 plan because it proposes to have the state pay the first 10 mills of property taxes on the first $20,000 of market value of homes belonging to people with adjusted gross incomes of $50,000 or less. The Blanchard Administration says it has created the plan because the local property tax is the state's most burdensome tax and because Michigan property taxes are among the highest in the nation. While some people get relief through the existing homestead property tax credit (the circuitbreaker) and everyone has benefited from recent increased state-level spending on education (which permits lower local property taxes), the administration believes more relief is needed and for more of the state's taxpayers. The governor has recommended the property tax cut be paid for by closing loopholes and ending tax preferences enjoyed by those who are not carrying their fair share of the state's tax burden, such as banks, domestic insurance companies, and utilities.

THE CONTENT OF THE BILL:

House Bill 4613 would amend the Income Tax Act to do the following:

- Create the 10/20 homeowner tax credit. The state would provide a taxpayer with an adjusted gross income of $50,000 or less with a credit equal to the first ten mills on the first $20,000 of market value ($10,000 of state equalized value) of his or her homestead; that means a tax credit of $100 (or less for a home with a market value of less than $20,000). The credit could be applied directly against property taxes, if a local collecting unit permitted, or could be taken as credit against the income tax. It would be a refundable credit. (House Bill 4605 would amend the General Property Tax Act to authorize local units, by resolution of the local legislative body, to let taxpayers apply the credit as a reduction in property taxes. The reduction would first be applied against a summer property tax levy.)
- Limit the homestead property tax credit (the circuit breaker) to those with household incomes under $50,000 (rather than $82,650 as is now the case). The credit would be reduced by ten percent for each claimant whose household income exceeded $41,000 (rather than the current $73,650) and by an additional ten percent for each increment of $1,000 above that. This would begin with the 1988 tax year.
- Tax military pay except compensation for service in the national guard or reserves and military retirement benefits.
- Withhold taxes from single lottery prizes of $600 or more, by treating the prize money as if it were compensation, the state lottery were an employer, and the prize winner were a lottery employee.
- Treat as taxable income the ordinary income portion of a lump sum distribution to the extent deducted from gross income for federal tax purposes.
- Eliminate from the Single Business Tax Act a credit equal to five percent of the property taxes paid to the state by railroads, telegraph companies, telephone companies, and other public utilities under Public Act 282 of 1905.
- Incorporate an increase in the personal exemption from $1,500 to $1,800 for the 1987 tax year, to $1,950 for 1988, and $2,000 thereafter. An additional exemption of $1,200 for 1987, $1050 for 1988, and $1,000 thereafter would be allowed for a paraplegic, quadraplegic, or hemiplegic; a deaf person; a person 65 years of age or older; a blind person; and for a return for which unemployment compensation amounted to 50 percent or more of adjusted gross income. (These provisions are also found in Senate Bill 8, the so-called windfall bill.)

MCL 211.44 et al. (House Bill 4605) and MCL 206.30 et al. (House Bill 4613)

House Bill 4610 would increase the intangibles tax on deposits in banks and savings and loan organizations to 40 cents per $1,000 from 20 cents per $1,000. The bill would be effective for taxes due after December 31, 1987.

MCL 205.132

House Bill 4606 would require federally insured banks to pay an additional intangibles tax of 75 cents per $1,000 of deposits for the calendar years 1987 through 1990. The banks could, however, claim a credit against the intangibles tax equal to the amount by which the additional tax exceeded 27.5 percent of the amount by which their single business taxes were reduced by the exclusion of income from obligations of the United States for the tax years ending prior to 1984 (because the U.S. Supreme

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Court forbade the states from taxing income from federal obligations while not taxing income from their own.)

MCL 205.132a

House Bill 4609 would amend the Insurance Code to make domestic insurance companies (those based in Michigan) subject to the tax of two percent (or three percent on fire, marine, and automobile insurance) on premiums, now levied only against foreign (out-of-state) insurers. Domestic insurers now pay only the single business tax. The bill would exempt from the premium tax the first $1 million of premiums. That exemption, however, would be reduced by $2 for each $1 by which the insurer's gross premiums exceeded $1 million. Fire, marine, and automobile premiums would be counted first toward the $1 million exemption, followed by life and casualty premiums. Domestic insurers would be subject to the premium tax beginning with the 1988 tax year.

MCL 500.440 et al.

House Bill 4607 would amend the Single Business Tax Act to exempt from the SBT insurance carrier services of a domestic insurance company subject to the premium tax (as foreign insurers are exempted). The bill would take effect January 1, 1988.

MCL 208.35

House Bills 4609 and 4607 are tie-barred to one another and to House Bill 4613.

House Bill 4608 would amend the General Sales Tax Act (MCL 205.51) to specify that computer software was subject to the state sales tax. House Bill 4612 would amend the Use Tax Act (MCL 205.92) to make computer software subject to the use tax. In each bill, computer software would be defined as a set of statements or instructions that when incorporated in a machine-usable medium was capable of causing a machine or device having information processing capabilities to indicate, perform, or achieve a particular function, task, or result.

The taxes would be on computer software offered for general sale to the public (or general use by the public) and software modified or adapted to the user's needs or equipment only if it was available on an as-is basis or as an end product without modification or adaptation. Not included under the taxes would be software originally designed for the exclusive and special needs of the purchaser and specific, separately identified, charges for technical support or for adapting or modifying software programs for the purchaser.

10/20 Homeowner Tax Credit

House Bill 4613 would create the 10/20 Homeowner Credit Reimbursement Revolving Fund out of which the Department of Treasury would reimburse the general fund for credits against the income tax, and local tax collecting units for credits against local property taxes. The reimbursements to local units would not be considered state spending under the Management and Budget Act or an expenditure under the state constitution. The fund's revenues would come from state income tax collections.

House Bill 4605 would require local units that elected to allow the 10/20 credit to be applied directly to local taxes to send a notice to all agricultural and residential property owners of the availability of the credit, along with a reduction form for use in applying for the credit with the treasurer of the local tax collecting unit. The notification could be sent with the assessment notice, but in any case could not be sent later than the assessment notice. The reduction form would have to be submitted by May 1. The local treasurer would have to send a reimbursement statement to the Department of Treasury by June 1 for summer tax levies and by November 1 for winter tax levies. The state treasurer would reimburse the local units by July 1 or December 1, respectively. Interest would accrue on late payments. The tax statement local units send to taxpayers would have to specifically show and identify the amount of a 10/20 credit applied against property taxes. If a tax statement was sent only to a taxpayer's designated agent, the agent would have to send a substantially similar statement to the taxpayer.

Each of the bills is tie-barred to House Bill 4613, and House Bill 4613 is tie-barred to all the other bills in the package.

FISCAL IMPLICATIONS:

The governor's proposal is intended to be revenue neutral. However, one of the bills from the original package, House Bill 4611, which would have repealed a property tax credit for railroads equal to 25 percent of the amount they spend maintaining or improving rights of way, was not reported from the House Taxation Committee. The value of that credit in 1985 was $7.5 million.

The property tax cut would cost $200 million, according to the Department of Treasury. The department says the same amount would be raised as follows:

Premium tax on domestic insurers	$55 million
Lower income ceiling for circuit breaker	$36 million
Tax on military pay	$25 million
Tax on lottery winnings	$24 million
Recoupment of 1983 bank windfall (over four years)	$18 million
Financial institutions tax	$13 million
Computer programs tax	$10 million
End to utility tax credits	$14 million*
Lump sum distributions	$ 5 million
Total	$200 million

*includes repeal of railroad right-of-way credit in House Bill 4611.

ARGUMENTS:

For:

The 10/20 plan would bring much-needed property tax relief to 2.15 million Michigan households, some 800,000 of which do not benefit from the circuitbreaker program. The plan cuts $200 million annually off property tax bills without any revenue losses to schools or other local units and makes up lost state revenue by raising taxes on those who the treasury department says have not been paying their fair share. The plan offers simple, immediate relief to 90 percent of the state's homeowners from the most inequitable and burdensome of taxes. Michigan, by most accounts, ranks among the top half dozen states in property tax loads. Increased state spending on education is helping to restrain property taxes, and the 10/20 proposal is a sensible and practicable next step.

The plan would close loopholes and end unfair preferences that keep financial institutions, banks, utilities, and others from paying their fair share of state taxes. Domestic insurance companies under the governor's proposal would pay the premium tax like their out-of-state competitors must rather than the much lower obligation they face under the single business tax. (A group of very small domestic insurers will receive a small business exemption.) The treasury department has said that domestic insurance companies paid under $1.2 million in single business taxes in 1984 (and less in 1985), which amounts to less than three percent

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of what their tax bill would have been if they were treated in the same way as their out-of-state competitors. (Tax specialists say that 11 of the 17 largest in-state insurers paid no single business tax in 1984.) Further, Michigan's unequal treatment of domestic and foreign insurers could be found unconstitutional in the future (as Alabama's has been by the U.S. Supreme Court), threatening all premium tax revenues.

The plan would return banks to their 1975 tax levels after a dozen years of unintended windfalls under the single business tax. The treasury department says banks have been paying far less in taxes in the years since the SBT was adopted than under the previous tax structure (by one estimate they paid 25 percent less in state tax in 1983 than in 1974 despite substantial growth in deposits). Michigan's bank taxes would remain substantially lower than comparable states. Banks would also have to repay the refunds they received from 1978-1983 as a result of a court decision that prohibited states from taxing interest on federal obligations but not on state obligations (as Michigan did). The plan also would make it state policy that sales of canned computer software should be taxed (as they were until a recent court decision). Michigan would join nearly all other states with income taxes in taxing military pay. Outdated utility credits would be eliminated. Lump sum distributions would be treated like all other pension income. Large lottery winnings would be taxed like other gambling winnings. To offer property tax relief to more people, those with high incomes would no longer qualify for the circuitbreaker.

Against:

It is disappointing that the governor should offer such a small and insubstantial property tax relief plan at a time when the property tax system and school financing methods are undergoing comprehensive scrutiny. The $100 (or less) relief per household will have little impact on property tax burdens, particularly since the 10/20 plan might encourage local units to raise property taxes and since the plan involves tax shifts that will put money in one pocket and take as much or more out of another. The plan simply does not address the basic problems associated with the property tax and complicates future tax deliberations by increasing the taxes of popular targets merely to find replacement revenues.

The plan repeats some of the tax increase proposals from the governor's property tax proposal of last session without taking into account changes wrought by the new federal tax law. Financial institutions and insurance companies, two targets of this package, say that they face considerably higher federal and state taxes as a result of the new law. The Michigan Bankers Association says the nine largest bank holding companies will pay $64 million in additional single business taxes to the state over the next ten years as a result of their treatment under the new federal act (and the MBA argues that banks in Michigan pay far more than in competitor states: the ten largest banks will pay $24.9 million in state taxes here but would pay only $6.4 million in Illinois). Insurance companies in the state (which by and large are relatively small companies by industry standards) say they will face an 80 percent increase in state taxes due to the Tax Reform Act of 1986. They further point out the extent to which they, unlike other businesses, support state guaranty funds and high risk pools in addition to their business taxes. If the legislature is concerned about discrimination in taxation of out-of-state and in-state insurance companies there are many ways the issue can be addressed that don't involve a mammoth tax increase for Michigan companies (and that recognize the need for retaliatory tax policies to protect domestic companies). The state's life insurers point out that the single business tax intended to encourage job-producing capital expenditures and yet they face criticism when their tax obligations are reduced through such economically beneficial behavior. Others who face higher taxes under this proposal have similar complaints. In some cases, higher taxes would be imposed on entities that already pay a lion's share, such as Michigan Bell. In general, the plan shifts taxes when tax cuts are what is needed. It will discourage business expansion in the state. Not only businesses are hurt by the plan, but many two-income homes will lose their eligibility for the circuitbreaker, despite the fact that at, say, $60,000 per year the families do not feel rich enough to be indifferent to the effects of high taxes.

Response: It should be pointed out that the 10/20 plan would not interfere with any current discussions about property tax reform and school finance restructuring. If anything it can be viewed as a down payment on comprehensive reform. (It should be noted that school finance reform has been a live issue for nearly 20 years.)

POSITIONS:

The Governor's Office and the Department of Treasury support the bills. (4-6-87)

Among the groups that testified against some portion of the proposal before the House Taxation Committee were: The Michigan Bankers Association; the Michigan Insurance Federation; The Michigan State Chamber of Commerce; the Greater Detroit Chamber of Commerce; Michigan Bell; and the Life Association of Michigan.