HOUSE FISCAL AGENCY

Personal Property Tax Reform

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Explanation of Terms

- **Property Categories:** Taxable property is generally either real property (land and structures) or personal property (machinery and equipment, furniture and fixtures, etc.).
- **Property Classifications:** Both real and personal property are typically classified as either residential, industrial, commercial, agricultural, or utility. Almost all personal property classified as residential (individual) or agricultural is exempt.
- **Personal Property Taxable Value:** Taxpayers report personal property by the new acquisition cost and date acquired to the local assessor. The taxable value is one-half of the depreciated amount (also known as true cash value).
- **Millage Rate:** 1 mill = $1 per $1,000 of taxable value. Millages can be levied for specific purposes (such as a dedicated police and fire or library millage) or for general operating purposes. The 6-mill State Education Tax (SET) is a millage rate levied by the state. Local millages are typically subject to renewals.

Background Information

- Although commercial and industrial personal property has generally been taxable, it has received some preferential treatment over the years.
- When the Single Business Tax (SBT) was enacted in 1975, inventories became exempt and were removed from the personal property tax base.
- When the Michigan Business Tax (MBT) replaced the SBT in 2008, industrial personal property was granted an exemption from the 6-mill SET as well as the 18-mill non-homestead levy. On average, this provided about a 40% reduction in personal property taxes levied on industrial personal property.
- The MBT also provided a credit for 35% of any remaining industrial personal property tax. This offset about one-third of any remaining taxes levied on industrial personal property.
- Commercial personal property was granted an exemption from the 6-mill SET and six of the 18 non-homestead mills.

Explanation of Terms – PPT Reform

- **Eligible Manufacturing Personal Property (EMPP):** Industrial and commercial personal property used at least 50% of the time for industrial processing or direct integrated support. Note that EMPP is defined by use rather than classification.
- **Direct Integrated Support:** Includes R&D, testing and quality control, engineering, and warehouse facilities that directly support industrial processing.
- **Municipality**: For the purpose of PPT reform, the term "municipality" is not limited to a local government such as a city, village, township, or county, but is essentially any entity that levies a millage. Taxing authorities such as community colleges, school districts, transit systems, senior centers, recreation districts, and libraries are all municipalities.
- **Essential Services**: Essential services are defined as ambulance, fire, and police services, jail operations, and funding pensions for employees that provide these services.

Legislative History of the PPT Phase-Out

- Originally enacted as Public Acts 397-404 and 406-408 of 2012.
- Amended by Public Acts 80, 81, and 86-93 of 2014.
- A local community stabilization authority (LCSA) was created to levy a portion of the state 4% use tax. The dollar amounts are specified in the use tax act, and are used by the LCSA to reimburse municipalities for the loss of personal property tax revenue.
- All the provisions were subject to a legislative referendum, which required a statewide public vote in August 2014 to permit the LCSA to levy a statewide local tax (to comply with Article IX, section 31 of the Michigan Constitution).
- A new Essential Services Assessment (ESA) is levied by the state against those taxpayers benefiting from the EMPP exemption to help offset the loss of use tax revenue that would have accrued to the general fund. The ESA generated almost $84.0 million in FY 2016-17, all of which accrued to the General Fund. The ESA is expected to generate about $120.0 million by FY 2027-28.

LCSA Use Tax Levy (in millions of dollars)

Fiscal Year	Use Tax Levy		Fiscal Year	Use Tax Levy
FY 2015-16	$96.4		FY 2022-23	$548.0
FY 2016-17	$380.9		FY 2023-24	$561.7
FY 2017-18	$410.8		FY 2024-25	$569.8
FY 2018-19	$438.0		FY 2025-26	$571.4
FY 2019-20	$465.9		FY 2026-27	$572.2
FY 2020-21	$491.5		FY 2027-28	$572.6
FY 2021-22	$521.3			

- After FY 2027-28, the amount will be determined by the Department of Treasury based on the prior year total, adjusted for the growth of personal property. Based on the current statutory language, the use tax levy will increase by 1% per year.

General Structure of the PPT Phase-Out

- There are two types of exemptions…the small taxpayer exemption and the exemption for eligible manufacturing personal property.
  - Beginning in 2014, a small taxpayer exemption was granted to taxpayers with commercial and/or industrial personal property with a true cash value less than $80,000. The taxpayer must file an affidavit (Form 5076) each year to claim the exemption.
  - Beginning in 2016, eligible manufacturing personal property (EMPP) acquired before 2006 as well as EMPP acquired after 2012 was immediately exempt. Like the small taxpayer exemption, taxpayers must report EMPP annually to their local assessors on Form 5278.
- Eligible manufacturing personal property acquired after 2005 and before 2013 will become exempt one year at a time. By 2023, all EMPP will be exempt.
- Municipalities will be reimbursed by the LCSA for their qualified losses, although 100% reimbursement is not necessarily guaranteed for all levies.

Distribution of Replacement Revenue

- Certain municipalities (Tier 1) are guaranteed 100% replacement for qualified losses. They include:
  - Essential services levies by cities, villages, townships, and counties
  - Any small taxpayer exemption loss
  - Local school districts (debt, sinking fund, recreation, and any operating loss not reimbursed by the School Aid Fund)
  - Intermediate school districts (all millages)
  - Tax increment finance (TIF) authorities

Distribution of Replacement Revenue

- Other municipalities with taxing authority (Tier 2) share any remaining replacement revenue. They include:
  - Non-essential services levied by cities, villages, townships, and counties (debt and operating losses)
  - Community colleges (debt and operating losses)
  - Libraries (debt and operating losses)
  - Other authorities (such as recreation, transit, sewer and water, etc.)
- These municipalities are not guaranteed 100% replacement for qualified losses if the remaining revenue is not sufficient to hold them harmless.
- In that instance, redistribution payments would be prorated.

Distribution of Replacement Revenue

- In the event additional funding remains after both Tier 1 and Tier 2 municipalities have received 100% replacement, Tier 3 payments are to be distributed to Tier 2 recipients in the same proportion as Tier 2 payments.
- Beginning in FY 2019-20, 5% of Tier 3 payments will be redistributed to Tier 2 recipients based on each municipality's share of its EMPP loss as determined using a modified acquisition cost definition of EMPP.
- Each subsequent year the percentage will be increased by 5% until Tier 3 payments no longer exist.

Distribution of Replacement Revenue
Small Taxpayer Exemption Loss

- The small taxpayer exemption loss for a municipality is its 2013 taxable value of commercial and industrial personal property minus the smaller of its 2014 or 2015 taxable value of commercial and industrial personal property.
- Each municipality's replacement payment is its small taxpayer exemption loss times the lowest millage rate between 2012 and the year immediately preceding the reimbursement.
- If a millage is allowed to expire and is then subsequently renewed, that municipality will no longer be eligible for a reimbursement.
- Millage increases after 2012 will not be considered for purposes of reimbursement.

Distribution of Replacement Revenue
Eligible Manufacturing Personal Property Loss

- The EMPP loss for an individual municipality is calculated as the 2013 taxable value of commercial and industrial personal property minus the current year taxable value of commercial and industrial personal property.
- For non-Tier 1 recipients, the small taxpayer exemption loss is subtracted to avoid double-counting.
- As with the small taxpayer exemption loss, each municipality's replacement payment is its EMPP loss times the lowest millage rate between 2012 and the year immediately preceding the reimbursement.

Example – City of Flint for TY 2017

- Flint's small taxpayer exemption loss = $13.9 million.
- The qualified EMPP loss = $35.0 million.
- Flint's total reimbursement = $1,414,682.42

Millage Name	Purpose	Millage Type	Lowest Millage	Essential Services Distribution	Small Taxpayer Exemption Loss	Qualified Loss @ 100%	Qualified Loss > 100%
Allocated/ Charter	General Operating	Part-ES	7.5000	$145,382.32	$104,435.29	$117,023.97	$225,233.30
Police/ Fire	Operating	ES	6.0000	$205,351.26	$83,548.23	$5,236.80	$10,079.15
Parks/Rec	Operating	Non-ES	0.5000	$0.00	$6,962.35	$17,421.59	$33,530.93
Police	Operating	ES	2.0000	$68,450.42	$27,849.41	$1,745.60	$3,359.72
Pub Imprv	Operating	Non-ES	2.5000	$0.00	$34,811.76	$87,107.93	$167,654.59
Transit	Operating	Non-ES	0.6000	$0.00	$8,354.82	$20,905.90	$40,237.10
TOTALS				$419,184.00	$265,961.86	$249,441.79	$480,094.79

Tier 3 Payments
(Qualified Loss > 100%)

- Tier 3 payments have been higher than originally anticipated in both TY 2016 and TY 2017. Only municipalities that receive Tier 2 payments are eligible for Tier 3 payments.

	TY 2016	TY 2017
Authorities/Libraries	$9.5	$13.5
Cities	$61.5	$66.7
Community Colleges	$15.4	$24.2
Counties	$26.2	$42.0
Townships	$5.6	$7.5
Villages	$2.5	$3.1
Total Tier 3 Payments	$130.7	$157.1

Tier 3 Payments

- Why have Tier 3 payments been so large?
  - In some instances, the amount of EMPP was simply less than anticipated.
  - Although personal property was growing, 2013 might have been a relatively low base against which to measure losses.
  - New commercial personal property growth mitigates a municipality's qualified EMPP loss, and in some instances completely offsets it. This reduces both Tier 1 and Tier 2 payments.

    A municipality's qualified EMPP loss is:

    $$2013\ TV_{\text{C\&I Personal Property}} - \text{Current Year } TV_{\text{C\&I Personal Property}}$$

- Such municipalities would not qualify for either Tier 2 or Tier 3 payments because they would have no qualified EMPP loss.
- Each municipality's Tier 3 payment is its share of total Tier 2 payments times the total amount of Tier 3 funding available.

Governor's Budget Proposal for FY 2018-19

- Eliminate the current distribution formula for Tier 3 payments.
- Distribute any available Tier 3 funding such that:
  - The first $15 million would fund Fire Protection Grants
  - Any remaining amount would be distributed as follows:
    - 48% to cities
    - 2% to villages
    - 5% to townships
    - 30% to counties
    - 15% to community colleges
- The distribution to cities, villages, townships, and counties would be on a per capita basis within each type of local unit.
- The community college distribution would follow the same percentage as the base appropriation.

This is all perfectly clear, right?

- Closing thoughts:
  - The small taxpayer exemption loss and EMPP loss are estimations based on the total taxable values of commercial and industrial personal property relative to TY 2013.
  - New development of non-exempt commercial property reduces a municipality's EMPP loss. If the development occurred in TY 2014 or TY 2015, the small taxpayer exemption loss could be reduced as well.
  - The PPT reimbursement process is very complex, and it's a zero-sum game.

For more information about PPT reform:

HFA website

https://www.house.mi.gov/hfa/PDF/Alpha/Ballot_Proposal_2014_1_Personal_Property_Tax_Summary.pdf

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