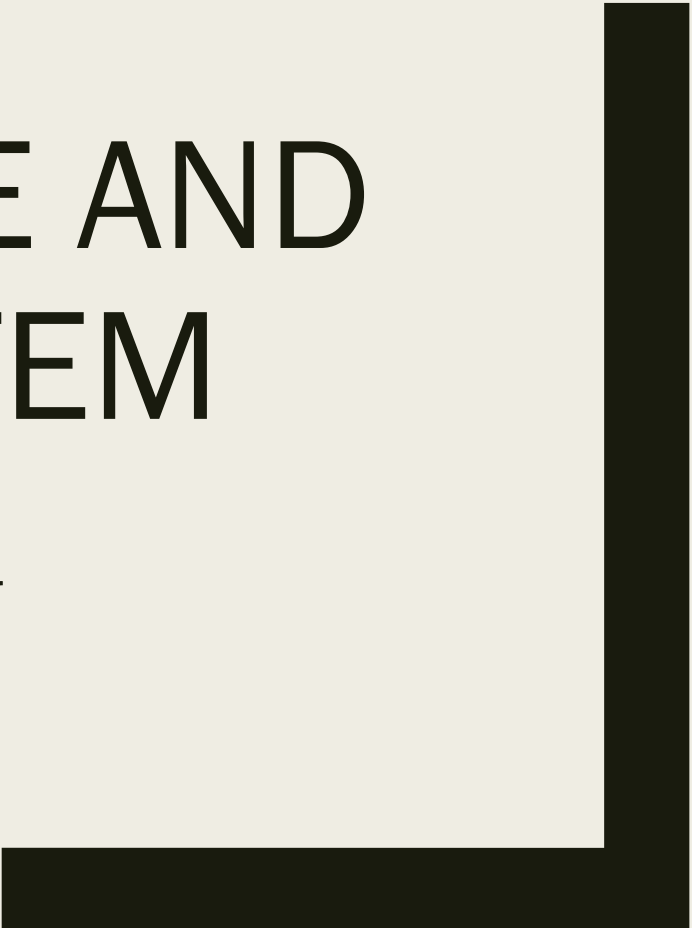




MICHIGAN'S STATE AND LOCAL TAX SYSTEM

Jeff Guilfoyle, Chief Deputy Treasurer
March 6, 2019



Michigan Treasury Responsibilities

Michigan Treasury has a wide range of responsibilities, including:

- State and local tax policy
- Economic and revenue forecasting
- Administration and collection of over \$24 billion in taxes and fees
- Pension Investment ~ \$65 billion in assets
- Local government and school financial health
- Higher education student financial assistance (MET, MESP)
- Managing the State's balance sheet
- Managing the State's relationship with Wall Street and rating agencies

Treasury's Path Towards Best Operated

Treasury has made important strides in improving the speed, fairness and effectiveness of administering the tax system; but there is still much work to be done.

Building Blocks:

- Continuous Improvement
- Culture of taxpayer service
- Employee Engagement

Recent Progress:

- Average audit time cut by more than half (356 days to 156)
- Income tax correspondence backlog reduced (12,000 to zero)
- Call wait times cut in half (5:27 minutes to 2:11)

Overall Taxes Paid By Michigan Taxpayers



Source: U.S. Census and IRS
Data are for FY 2016

Michigan Taxing Authority

■ State

- *Constitutional: property tax, sales tax, fuel tax usage, some restrictions on income tax*
- *Statutory: income tax, oil and gas, alcohol, tobacco, estate, lottery, motor vehicle registration*

■ Local

- *Constitutional: property*
- *Statutory: income*

Constitutional Taxing Provisions

- Income Tax

- *Prohibits graduated rate or base*

- Sales Tax

- *Sets maximum rate at 6%*
- *Earmarks 73% to education*
- *Earmarks 10% to cities, townships, and villages*
- *Exempts food and prescription drugs*

- Motor Fuels

- *Restricts for transportation purposes*

Constitutional Taxing Provisions

■ Property Tax

- *Sets maximum rate for certain millages*
- *Limits assessment to 50% of true cash value*
- *Limits assessment increases to inflation, values pop back up after sale*
- *Millages fall when assessments grow by more than inflation (excluding new construction)*
- *Requires 3/4 vote of legislature to raise school operating taxes*

■ Revenue Limit

- *Restricts total state revenues to a fixed share of the State's personal income*

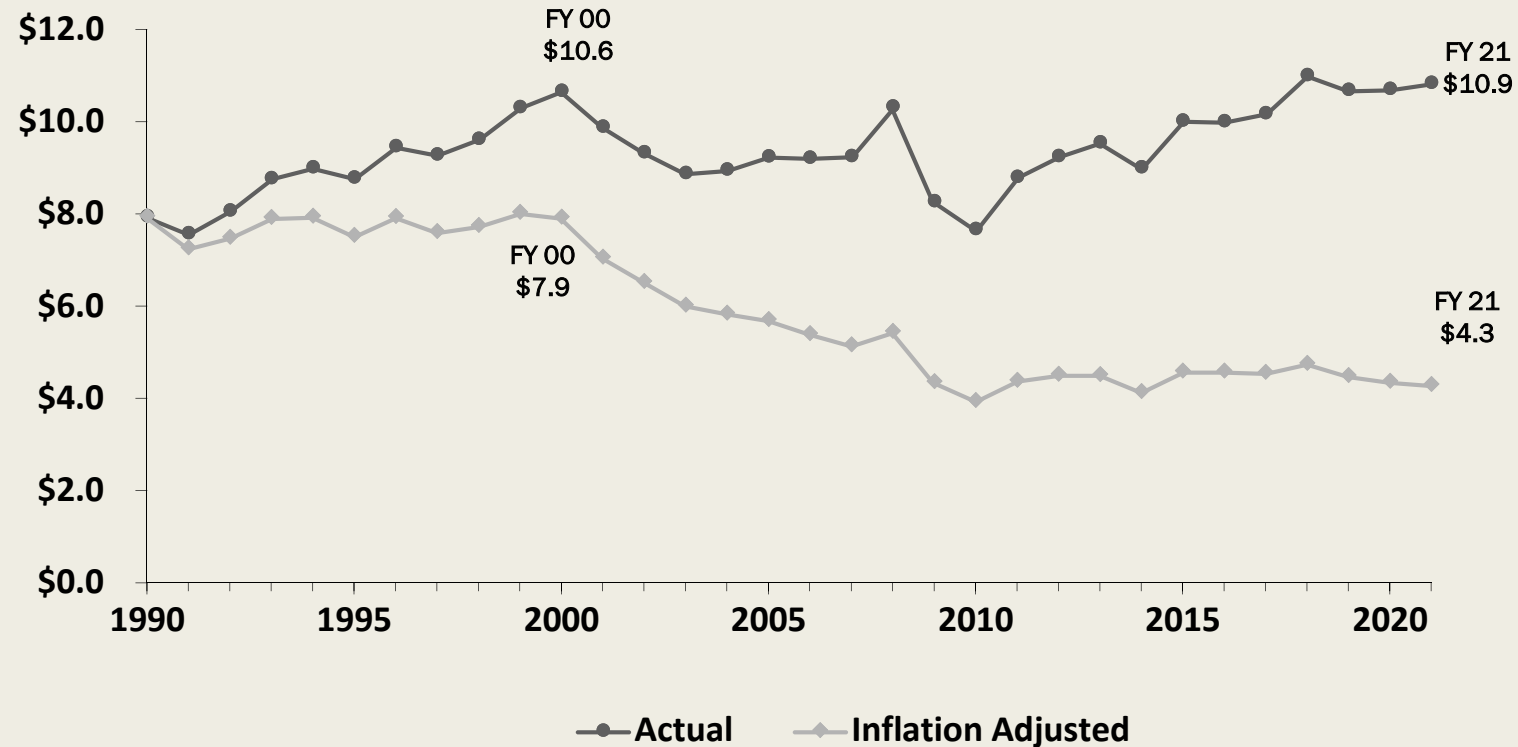
State and Local Taxes Generate \$40 billion in FY 2018 ~ Big Three Counts for 85%

The Big Three	FY 2018 Est. Amount	Tax Rate	Fund
Income Tax	\$10.2 billion	4.25%	General Fund (72%) School Aid Fund (28%)
Sales/Use Tax	\$ 9.5 billion	6.0%	General Fund (21%) School Aid Fund (69%) Revenue Sharing (9%)
Property Tax (State and Local)	\$14.0 billion	varies	Local Units (86%) School Aid Fund (14%)
Other			
Corporate Income Tax (CIT)	\$1,016 million	6.0%	General Fund
Michigan Business Tax (MBT)	(\$646 million)	Mostly credits	General Fund
Transportation (Gas, Diesel, MV Registration)	\$ 2.8 billion	26.3 cents per gallon value of vehicle	Michigan Transportation Fund
Tobacco Tax	\$ 920 million	Cigarettes \$2/pack; other 32% wholesale price	General Fund School Aid Fund Medicaid Trust Fund Other Funds
Other/Miscellaneous	\$ 1.8 billion	varies	General Fund School Aid Fund

General Fund Revenue Flat Since 2000

GF-GP Revenue: Actual & Inflation Adjusted

(billions)



Major General Fund Revenues FY 2018

Income tax	\$7.3 billion
Sales & Use	\$2.1 billion
Insurance	\$393 million
CIT/MBT	\$370 million
Cigarette	\$181 million
Other taxes	\$295 million
Non-Tax Revenue	<u>\$419 million</u>
TOTAL	\$11.0 billion

Note: GF-GP figures are presented on a Consensus basis. FY2019-FY2021: Jan 2019 consensus estimates

Prepared by: Office of Revenue and Tax Analysis, Michigan Department of Treasury

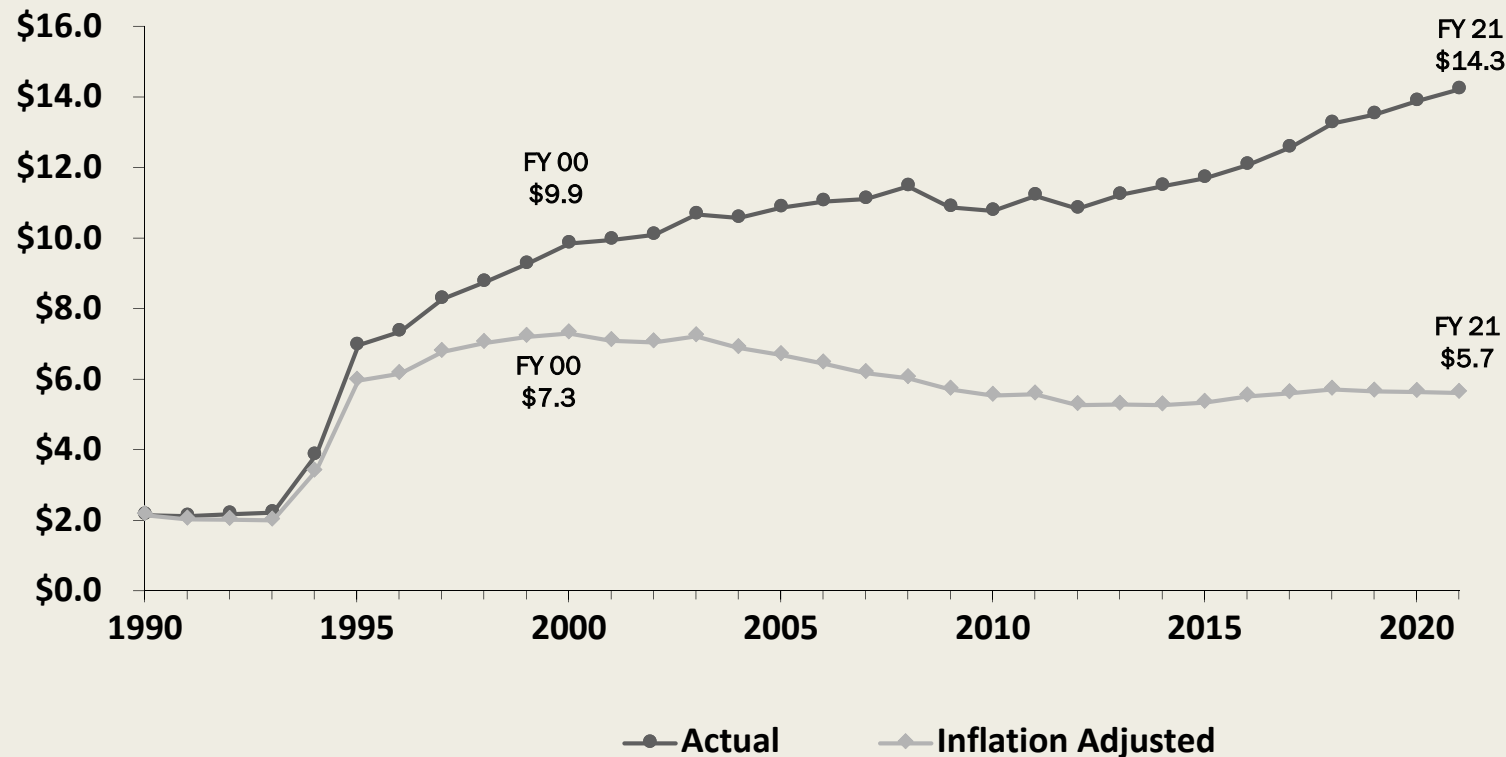
School Aid Fund (SAF) Up 34% since 2000 (due to income tax and lottery revenue growth)

Major School Aid Fund Revenues FY 2018

Sales & Use	\$5.9 billion
Income Tax	\$2.9 billion
Property Tax	\$2.0 billion
Lottery	\$980 million
Cigarette	\$344 million
Real Estate	\$350 million
Other taxes	<u>\$234 million</u>
TOTAL	\$13.3 billion

SAF Revenue: Actual & Inflation Adjusted

(billions)



Note: SAF figures are presented on a Consensus basis. FY2019-FY2021: Jan 2019 consensus estimates

Prepared by: Office of Revenue and Tax Analysis, Michigan Department of Treasury

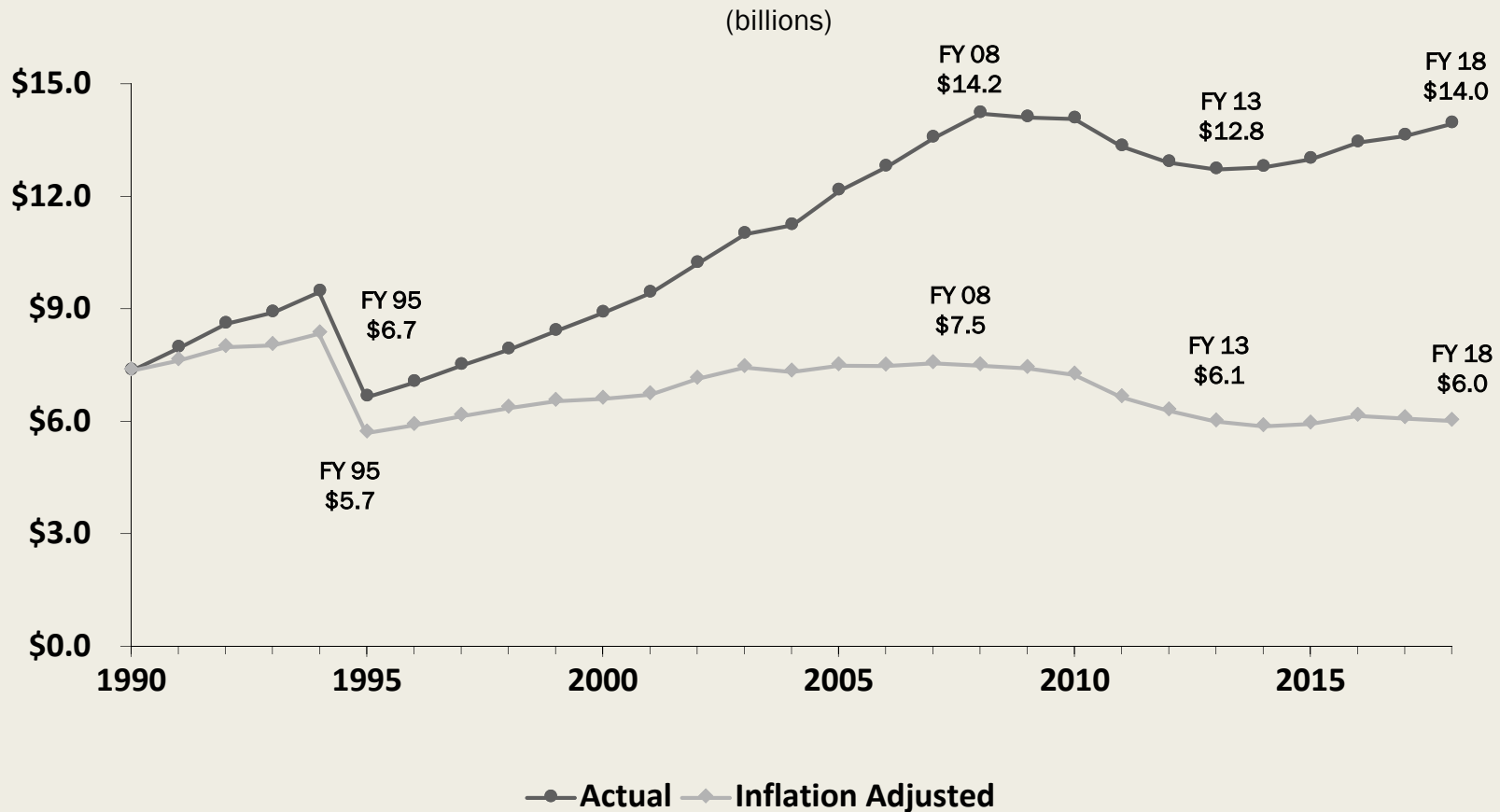
SAF - Higher Education Support

- In FY 2019, \$908.3 million SAF dollars are used to support community colleges and universities.
- This amount has increased in recent years.
- Additional general fund dollars would be necessary to shift this \$908.3 million back to the K-12 budget, if the same level of state support for community colleges and universities is maintained.

Fiscal Year	PreK-12	Community Colleges	Universities
2009	\$11,019.8	\$0.0	\$0.0
2010	\$10,644.9	\$208.4	\$0.0
2011	\$10,784.8	\$0.0	\$0.0
2012	\$11,010.2	\$259.6	\$200.0
2013	\$10,928.6	\$197.6	\$200.5
2014	\$11,200.2	\$197.6	\$200.5
2015	\$11,814.1	\$364.7	\$206.5
2016	\$11,905.4	\$256.7	\$205.2
2017	\$12,069.6	\$260.4	\$237.1
2018	\$12,686.3	\$398.3	\$238.3
2019	\$12,876.8	\$408.2	\$500.1

Property Tax Dominates Local Government Revenue

Property Tax Revenue: Actual & Inflation Adjusted



Major Local Government Revenue Sources

Property Tax	\$12.0 billion
Revenue Sharing	\$ 1.2 billion
Income Tax	\$533 million
Casino	\$183 million
Utility	\$ 60 million
Other	<u>\$338 million</u>
TOTAL	\$14.3 billion

Policy Changes Impact Revenue

GF use tax earmark to the Local Community Stabilization Authority:

- Began in FY 2016
- \$410.8 million in FY 2018
- \$438.0 million in FY 2019

Transportation earmark from personal income tax begins in FY 2019

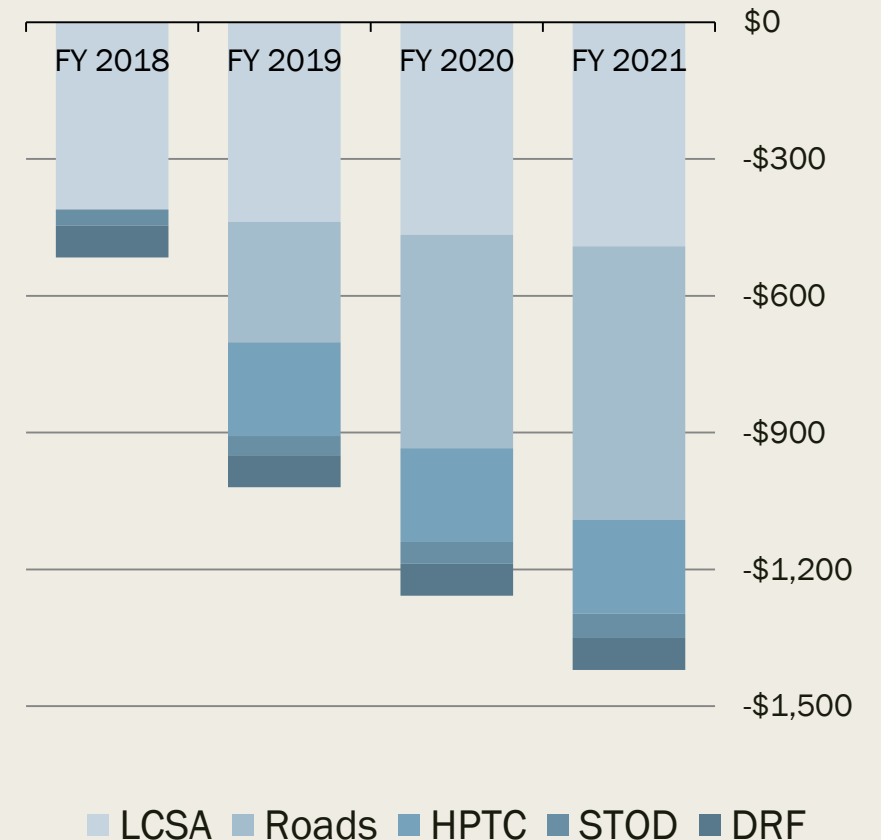
- \$264 million in FY 2019, \$468 million in FY 2020, \$600 million in FY 2021

Homestead Property Tax Credit will be expanded and cost over \$200 million per year beginning in FY 2019

“Sales Tax on the Difference” for purchases with trade in vehicles increases by \$35 to \$48 million per year

Driver Responsibility Fees eliminated

- FY17 collections total about \$70m



Transportation Funding Reform Provided Some New Funding for Roads - Significant Share is from the General Fund

Transportation Taxes

- Gas tax increased 7.3¢/gallon
- Registration fees increased 20% effective 1/1/2017
- General Fund Income tax earmark to MTF FY 19 \$264 million, FY 2020 \$468 million, FY 2021 & later \$600 million
- Homestead property tax credit increased by \$200 million beginning in FY 2019
- Income tax rate declines when GF revenue grows faster than inflation times 1.425, effective FY 2023.

Tax	Dollars in Millions		
	FY 2017	FY 2018	FY 19-FY28
Motor Fuel	\$328	\$428	\$4,260
Vehicle Registration	\$150	\$195	\$2,315
General Fund IIT Earmark	\$0	\$0	\$5,275
New Transportation Revenue	\$478	\$623	\$11,850
Income Tax Changes			
Property Tax Credit Increase	\$0	\$0	(\$2,269)
Tax Rate Reduction Trigger	\$0	\$0	(\$2,536)
Net IIT Cut	\$0	\$0	(\$4,805)

Michigan's Tax Burden Declined Relative to Other States

Tax Category	All 50 States		5 Great Lakes States
	2010	2016	2016
U.S. Census Bureau ¹⁾	<i>1 is highest</i>		
Total State & Local Taxes	18	31	4
Personal Income Tax	34	31	4
Sales Tax	25	30	3
Property Tax	11	17	3
Corporate Income/MBT	6	45	4

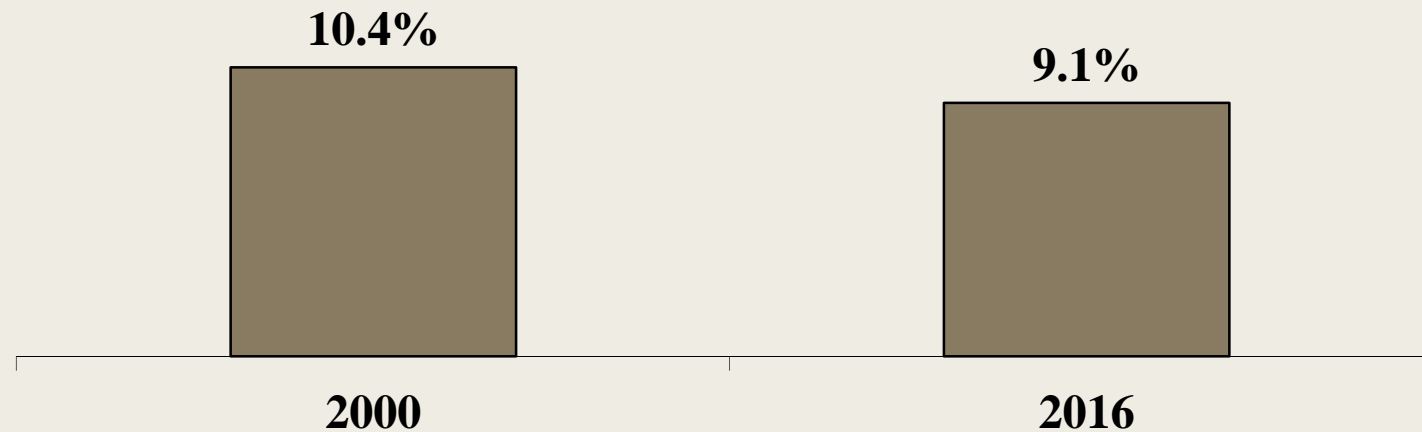
1) U.S. Census Bureau, Government Finances: Based on State and Local Taxes as a percentage of personal income.

Michigan Taxes

- Michigan ranks 31st (1 is highest) in total state and local tax burden in 2016.
- Among the five Great Lake States, Michigan has second lowest tax burden.
- Michigan's ranking is down from 18th in 2010.
- Michigan property tax ranks 17th and CIT/MBT ranks 45th.

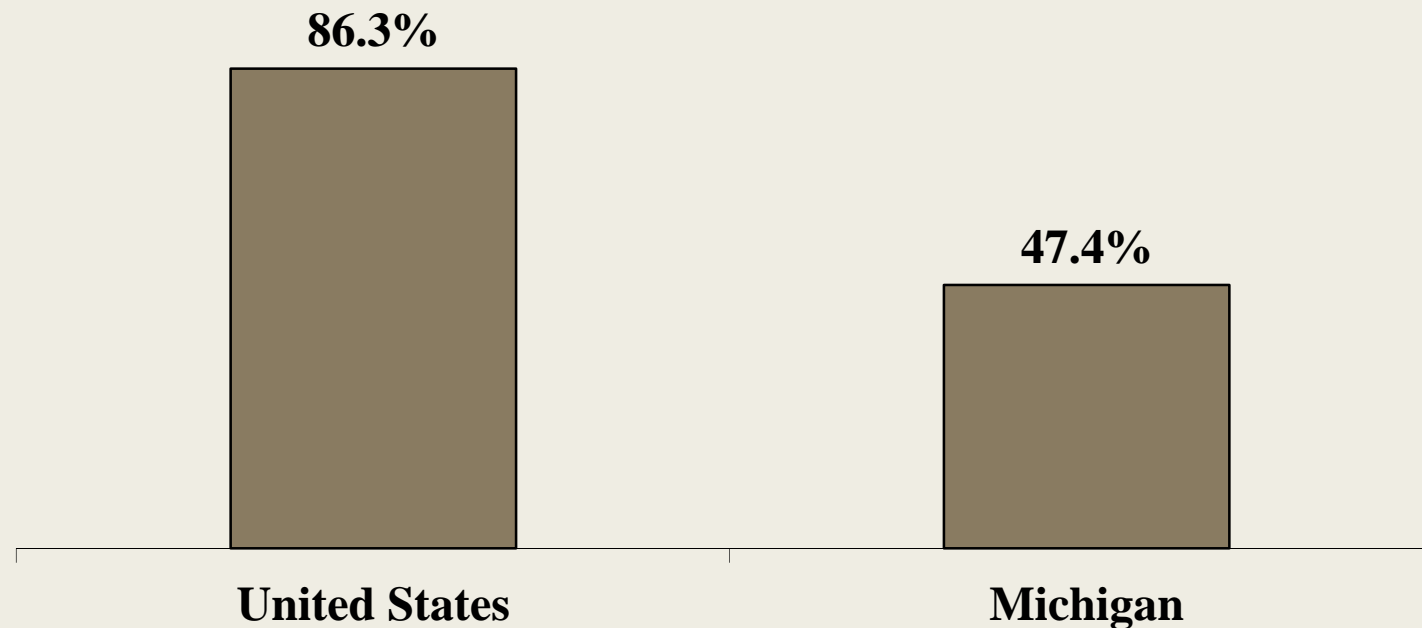
Michigan Taxes Have Fallen as a Percent of State Income

Taxes as a Share of State Personal Income



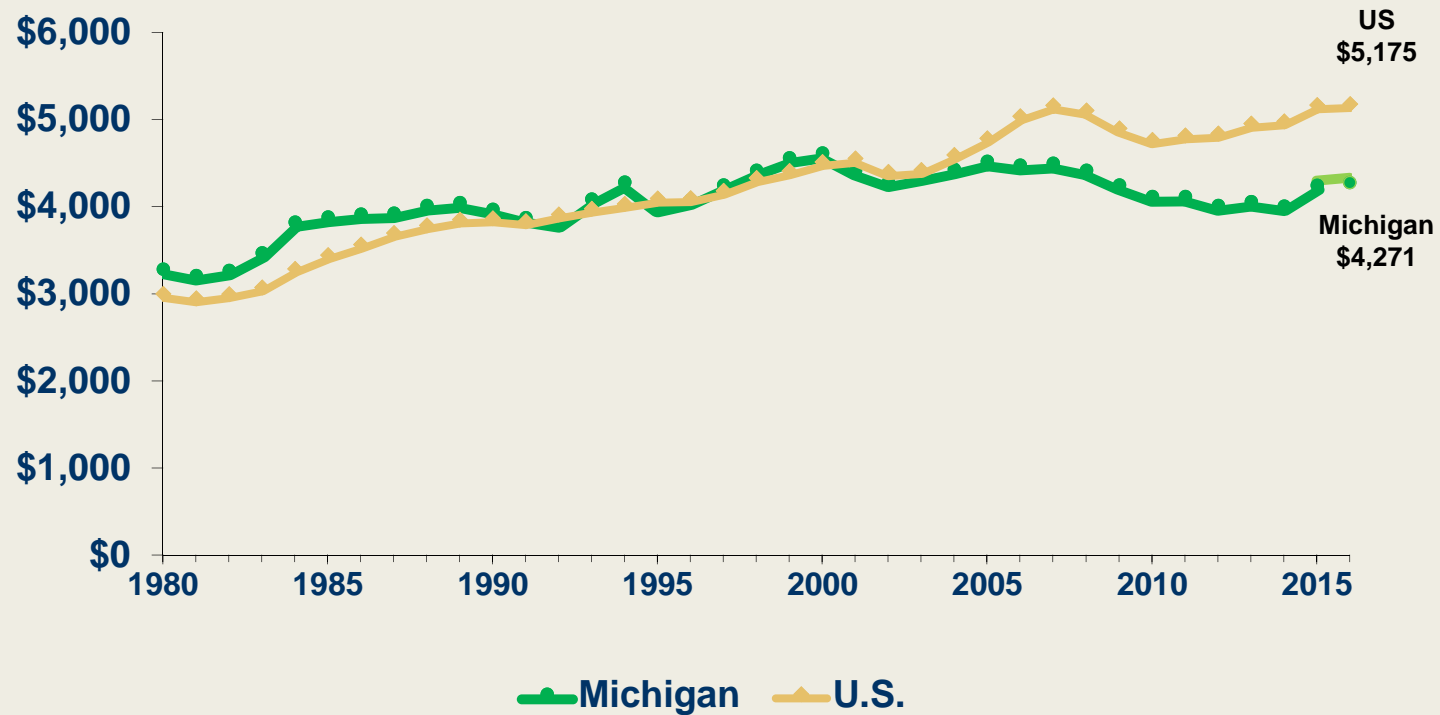
Income Growth has Large Impact on Revenues

Personal Income Growth 2000-2016



Michigan Trails U.S. in State and Local Taxes Per Capita

2018 Dollars



Source: Michigan Department of Treasury & Bureau of the Census

Tax Changes Included in FY 2020 Budget Proposal

- Increase gasoline tax by \$0.15 in October 2019, April 2020, and October 2020 for a total of 45 cents—raises \$2.5 billion in new revenue
- Double the earned income tax credit from 6% of federal credit to 12% (4% increase in FY 2019 and 2% increase in FY 2020)
- Create an entity level tax on pass through entities and use revenue to fund a repeal of the tax added to retirement income in 2011

Pass Through Entity Taxation

- Taxes pass through entities at the entity level instead of at the individual income tax level
- New rate of 6%, same as the C corporation rate, instead of 4.25%
- Taxing at entity level frees these businesses from the \$10,000 cap on the federal individual income tax deduction on state and local taxes—many taxpayers will see their combined state and federal tax fall
- Deduction of \$50,000 from income against entity level tax for all businesses helps to protect small businesses from increase

Restoring the Retirement Deduction

- Proposal would return Michigan's tax treatment of retirement income to 2011 law
 - *All benefits tax-free for public retirees*
 - *Private benefits (IRAs, qualified employer plans) deductible up to \$52,808 if single, \$105,615 for a married couple*
- Taxpayers born after 1945 would be able to choose to continue taking the deduction against all income at age 67, protecting seniors who continue to work from a tax increase
- The reduced taxation of retirement benefits would help ensure retirees are not burdened by additional gas tax