



CRC MEMORANDUM



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STATEWIDE BALLOT ISSUE: PROPOSAL 15-1

SALES AND MOTOR FUEL TAX INCREASES RELATED TO TRANSPORTATION FUNDING

Summary

The full paper can be found at www.crcmich.org/PUBLICAT/2010s/2015/transportation_funding_proposal.html

On May 5, 2015, Michigan voters will be asked to vote on a single statewide ballot measure to amend the state Constitution: Proposal 15-1. Approval of Proposal 15-1 will result in increases in various state taxes, expansion of state tax credits, additional state funds for road repair and maintenance, and additional state funds for public schools and local governments. Of some confusion, perhaps, is that voters are only being asked to directly approve *some* of these changes; those amending the Constitution. The bulk of the other state tax changes are contained in laws passed last legislative session that would only take effect if Proposal 15-1 is approved.

At the end of the 2013-2014 legislative session, the governor and legislative leaders agreed to a complex plan to address the dual objective of increasing state funding for road repair and maintenance and modifying the taxation of motor fuels to guarantee that all taxes paid at the pump were directed to transportation purposes. Additionally, the plan seeks to ensure that other recipients of state funds are not financially harmed in the pursuit of these two

primary goals. By necessity, the plan consists of both constitutional and statutory components.

While the statutory law changes require only legislative and gubernatorial approval, the constitutional changes require approval by the Michigan electorate. However, because the law changes are "tie-barred" to passage of Proposal 15-1, the public vote effectively serves as a referendum on the entire transportation funding package, both the constitutional and statutory changes. Voters are being asked to *directly* approve changes to the Constitution and *indirectly* approve changes in various state laws to implement the complex transportation funding plan.

If voters approve Proposal 15-1, the state Constitution will be amended and various state laws will take effect to increase state tax revenue by nearly \$2.1 billion next fiscal year and by \$1.8 billion annually in the following two fiscal years. If voters reject Proposal 15-1, there will be no changes to the Constitution and none of the proposed tax changes contained in the state laws linked to the proposal will take effect.

Changes Impacting Road Funding and Transportation

Proposal 15-1 and the various laws tie-barred to the proposal can be divided into three main issues or categories of change. First, the proposal modifies the taxation of gasoline and diesel fuel. This is accomplished by exempting these fuels from the sales tax base and changing how the state per-gallon motor fuel tax is calculated. The combination of these tax changes will likely increase the overall taxes paid at the pump. In combination, these changes are expected to bring in \$1.3 billion per year in additional revenue for road repair and maintenance

and other transportation purposes. This would be accomplished through statutory and constitutional changes that:

(Changes to the constitution, which require voter approval and are included in Proposal 15-1, are emphasized in blue)

1. Exempt gasoline and diesel fuel used to power vehicles on public roads from the sales and use tax;
2. Increase the state's motor fuel tax rates



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(currently 19 cents per gallon for gasoline and 15 cents per gallon for diesel fuel) to equal 14.9 percent of the recent wholesale price of each fuel. Initial per-gallon rates would be 41.7 cents for gasoline and 46.4 cents for diesel motor fuel;

3. Establish a floor and ceiling for motor fuel tax rates that allow for annual inflationary increases to the rates and limit the volatility

of future rate changes in response to future swings in wholesale fuel prices; and

4. Increase vehicle registration revenues by eliminating the depreciation discount currently given to passenger vehicles in the first few years; increase registration taxes on large trucks; and establish a new registration tax surcharge for electric vehicles.

Changes to Restore Funding from Sales Tax Exemptions

The transportation funding package proposes to eliminate fuel from the base of the sales tax. Portions of the revenues from the sales tax flow into the state’s General Fund and others are dedicated to the School Aid Fund and state revenue sharing to local governments. As a result, there would be less state funding available to these programs. The second major category of change associated with Proposal 15-1 and the linked state laws deal with modifications to the sales and use tax rates and how revenue from these taxes is distributed to hold these programs harmless. Because the state Constitution limits the maximum sales tax rate that can be levied, changes involving the tax rate require voter approval.

Overall, changes to the sales and use taxes are expected to generate an additional \$795 million per year for public schools, local governments, and the General Fund. These changes propose to:

5. Increase the maximum authorized rate of the sales tax from 6 percent to 7 percent;
6. Increase the use tax rate from 6 percent to 7 percent;
7. Dedicate 15 percent of the sales tax revenue collected at a rate of up to 5 percent (currently 4 percent) for per-capita allocations to cities, villages, and townships;
8. Dedicate 60 percent of the sales tax revenue collected at a rate of up to 5 percent (currently 4 percent) to the School Aid Fund; and
9. Dedicate 12.3 percent of the use tax revenue collected at a rate of up to 5 percent to the School Aid Fund (currently no portion of the tax levied at 4 percent is dedicated to the School Aid Fund).

Changes to Ensure Accountability of New Funding and Help those Most Impacted by Tax Increases

Finally, a number of other legislative and constitutional changes are included to address concerns regarding collateral impacts caused by tax increases and changes to revenue distributions. These proposed changes would:

10. Modify the allowable uses of the School Aid Fund to exclude higher education and include public community colleges, career and

technical education programs, and certain community college or career and technical education program scholarships;

11. Introduce new road construction and maintenance bidding, warranty, and road design guidelines to help ensure that new road funding is spent efficiently;
12. Increase the state’s Earned Income Tax Credit

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(EITC) for low-income tax filers in an effort to help offset the regressive nature of the tax increases; and

- 13. Expand the state’s Homestead Property Tax

Credit for very low-income senior citizens and disabled homeowners in an effort to help offset the regressive nature of the tax increases.

Impact on the Public Sector

CRC estimates that Proposal 15-1 will increase sales and use tax revenues by \$795 million in Fiscal Year 2016 (FY2016), with slightly less revenue collected in FY2017 and FY2018. The revenue increase will mean additional funding for the School Aid Fund, revenue sharing to local governments, some public transit programs, and the state’s General Fund.

Net revenue gains from motor fuel tax changes designed to increase road and transportation funding are estimated to be around \$1.3 billion in FY2016, with marginally more revenue raised in FY2017 and FY2018. For the first two years, \$860 million and \$460 million, respectively, of the additional revenue is dedicated by law to pay down past state transportation borrowing and the

remaining funds will be allocated to state and local road agencies and public transit programs through the transportation distribution formula. Initial indications are that these new revenues are viewed by state policymakers as easing pressures on the state’s General Fund by allowing funds currently appropriated for transportation improvements to be redirected to other purposes. Currently, \$285 million from the state General Fund is being used to subsidize dedicated transportation funding and allow for additional road repair and maintenance. If Proposal 15-1 is approved, a portion of the \$1.3 billion revenue gain will be used to supplant the General Fund resources going to road repair, thus easing pressures on the General Fund budget and reducing the net gain in road funding.

Impact on Michigan Citizens

How Proposal 15-1 and related legislation impact the amount motorists pay at the pump will depend on the price of fuel. At current prices (roughly \$2.40 per gallon in March 2015), constitutional and legislative changes would result in a 10.2 cent increase in the per-gallon price of gasoline with the tax rates to be levied in FY2016. Perhaps counterintuitively, as the price of gasoline increases the difference between what consumers pay under the current system and what they would pay under the proposed system shrinks. For example, if per-gallon gasoline prices

rise to \$3.85 during FY2016, consumers will only pay 2.1 cents per gallon more under Proposal 15-1 (See **Table A**).

Michigan’s citizens will also be obliged to pay a seven percent sales tax on goods subject to the tax; a one percentage point increase from the current rate of six percent. The impact of this will vary by individual but sales taxes tend to have a greater cost impact on lower-income individuals and families who spend proportionally more of their income on taxed goods

than higher-income individuals and families. Therefore, the proposal includes an increase in the state’s Earned Income Tax Credit as well as the Homestead Property Tax Credit for very low-income seniors and disabled homeowners.

Table A
Initial Impact of Tax Changes at the Pump

Pre-Tax Retail Price	Per-Gallon Cost					
	\$1.90		\$2.50		\$3.25	
	<i>Current</i>	<i>Proposal</i>	<i>Current</i>	<i>Proposal</i>	<i>Current</i>	<i>Proposal</i>
Federal gasoline tax	\$0.184	\$0.184	\$0.184	\$0.184	\$0.184	\$0.184
State sales tax	\$0.125	\$0.000	\$0.161	\$0.000	\$0.206	\$0.000
State gasoline tax	\$0.190	\$0.417	\$0.190	\$0.417	\$0.190	\$0.417
<i>Tax Subtotal</i>	<i>\$0.499</i>	<i>\$0.601</i>	<i>\$0.535</i>	<i>\$0.601</i>	<i>\$0.580</i>	<i>\$0.601</i>
Final Pump Price	\$2.399	\$2.501	\$3.035	\$3.101	\$3.830	\$3.851
	10.2 cent increase		6.6 cent increase		2.1 cent increase	

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