Michigan's Broken Model of Fiscal Federalism

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Citizens Research Council of Michigan

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State Revenue Sharing

The mismatch between tax collection efficiency and service delivery responsibility

- Taxes are best levied and collected across a wide geography
  - Minimizes need/desire to change economic behavior
- In Michigan, services delivered by local governments
  - Cities and townships have primary government responsibilities
  - Villages have secondary responsibilities
  - Counties serve recordkeeping, public safety, criminal justice roles
- How to get resources to the governments providing the services?

Michigan's State Revenue Sharing Program

- **Constitutional revenue sharing**
  - Initiated with 1946 constitutional amendment
  - Distributed on per capita basis
  - Change possible only with another amendment
- **Statutory revenue sharing**
  - Incrementally grown over the years
  - At one time larger than constitutional SRS
  - For 40+ years formula attempted to equalize tax capacity

Why Should the State Care if Local Governments Receive State Revenue Sharing?

- Local government hosts people and businesses upon which state taxes are levied
- Improving the overall state and local tax structure
- Promoting economic development
- Local governments provide services for the health and safety of Michigan residents and guests
- Maintaining acceptable levels of government services from community to community

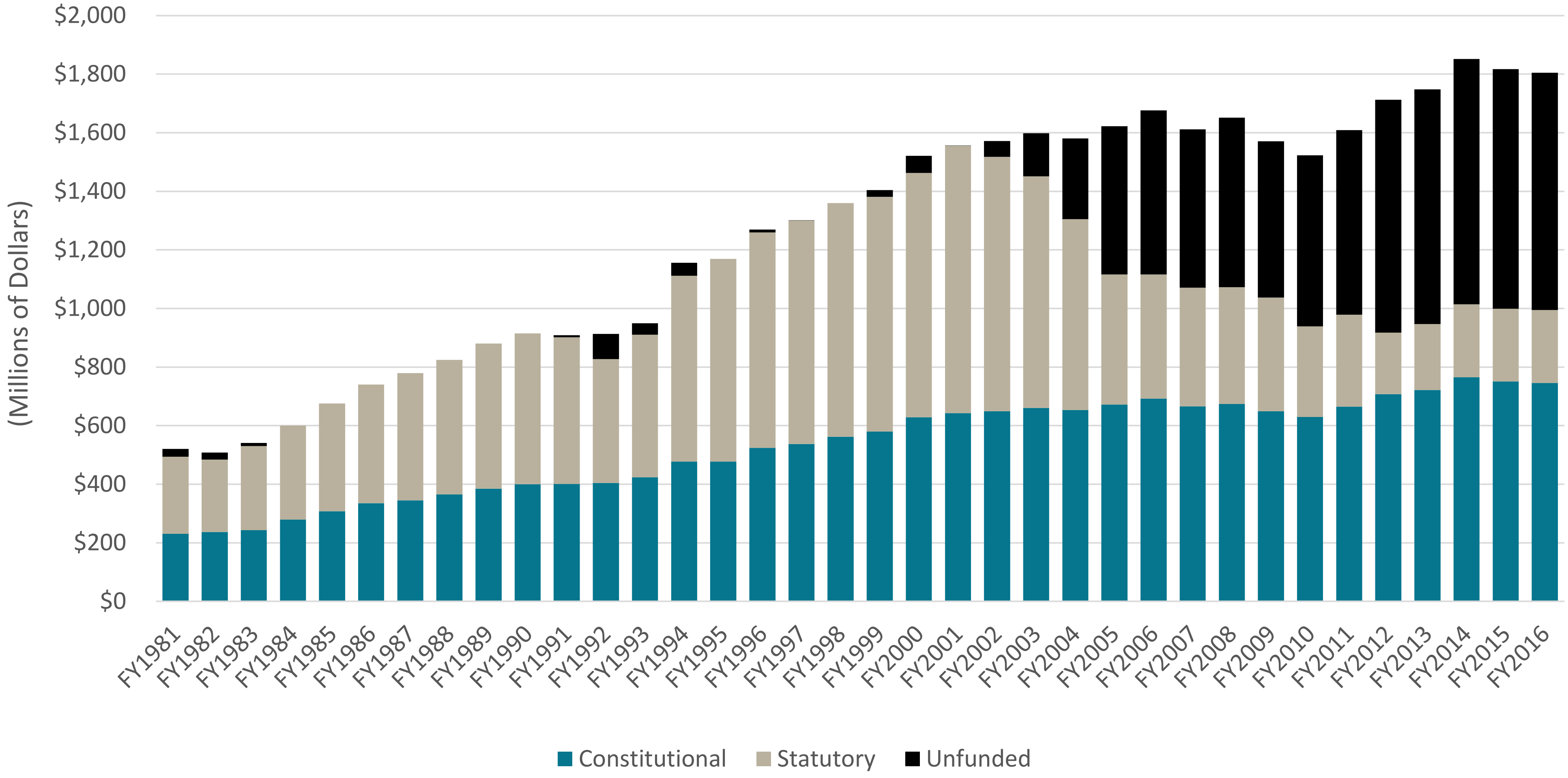
Why do we have Statutory State Revenue Sharing?

- Not <u>State Aid</u>
  - Would imply state revenues sufficiently plentiful that they could be put to good use helping the finances of local governments.
  - Would assume that local governments were in need of assistance and since each revenue sharing distribution was designed to send funding to all units of local government, that all local governments were in need of assistance.

Why do we have Statutory State Revenue Sharing?

- A series of agreements made over the years in which state policymakers agreed to serve in a revenue raising capacity for local governments
  - Capitalize on revenue raising capabilities
  - Share state-collected revenue with local governments
- State has adopted policies to distribute revenues to local governments for two purposes:
  - The replacement of revenue after certain local taxes were either discontinued or preempted by the state
  - To supplement local government revenue and general funds

Recent History



So the state cut revenue sharing dollars… and then what happened?

- Emergency Manager Law strengthened
  - Hurt cash flow
  - Little latitude to make up for lost revenue from other sources
  - Counter Intuitive Response
    - Forfeit democratic rights to state appointed EM
    - Task is to bring balance by cutting services and costs
    - In the end makes communities less attractive to live and work
- Economic Vitality Incentive Program instituted
  - Online dashboard, new inter-local collaboration, plan to fund legacy costs to qualify for statutory state revenue sharing distributions
  - One of few programs where state has leverage to affect behavior
  - Program runs counter to creation and intent of revenue sharing

Unfunded State Mandates

Mandates that do not Qualify for Protections against Unfunded Mandates

- Article IX, Section 29, prohibits the State from
  - mandating local governments to provide new services or activities (after 1978) without proper funding;
  - increasing the level of mandated activities and services required beyond what was required in 1978 without proper funding; or
  - decreasing the level of funding provided in 1978 for existing mandates.
- Courts have adopted narrow definition argued by state to disqualify requirements commonly accepted as mandates
  - If it is not required of all governments of that type (counties, cities, townships, villages, schools, etc.), it is not a mandate
    - Firefighters gear
    - Landfill protections against contamination
    - Training of local corrections officers

Article IX, Section 30

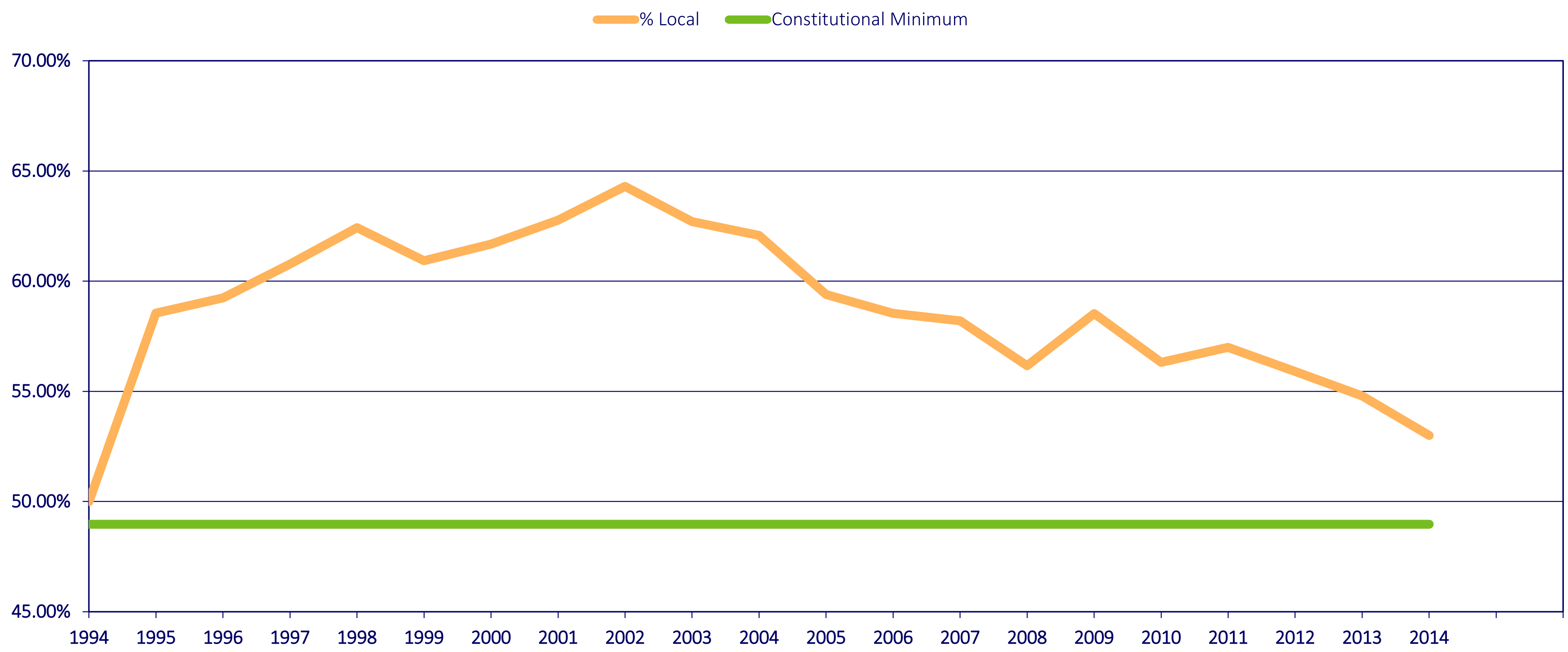
Headlee Amendment of 1978

Headlee Amendment: Article IX, Section 30

§ 30 Reduction of state spending paid to units of local government.

Sec. 30
The proportion of total state spending paid to all units of Local Government, taken as a group, shall not be reduced below that proportion in effect in fiscal year 1978-79.

Article IX, Section 30 State Spending



Taxpayers for Michigan Constitutional Government vs State of Michigan

- Lawsuit alleges that the state has violated Article IX, Section 30 because of erroneous accounting
  - Proposal A was a tax shift that should not be counted as state spending
  - Charter schools do not meet definition of local government
  - State contracts with local governments to care for state trunkline roads should not be counted as payments to local governments
  - Payments to fund mandates should not count toward this responsibility

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