CITIZENS RESEARCH COUNCIL OF MICHIGAN

"The right to criticize government is also an obligation to know what you're talking about."
Lent Upson, First Director of the Citizens Research Council

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Detroit Could Use Incremental Income Tax Revenue to Reduce the Property Tax

In a Nutshell

- Detroit's income tax revenue is projected to increase by 13.8 percent between FY2024 and FY2028.
- Updated estimates project approximately $95.7 million more in income tax revenue compared to earlier revenue projections.
- Incremental income tax revenue increases could be used to offset property tax cuts.

Earlier this month, the City of Detroit established its economic forecast and revenue projections for Fiscal Year (FY)2024 to FY2028. Between FY2024 to FY2028, Detroit projected it would collect $6.8 billion in General Fund revenue. Notably, income tax revenue has exceeded expectations. In February, the city projected it would collect $374.7 million in FY2023, and preliminary estimates from September are that Detroit collected $396.5 million in FY2023—$21.8 million (or 5.8 percent) more revenue. As income tax revenue increases, incremental improvements between forecasts, such as the $21.8 million in unanticipated revenue, could be earmarked to offset a cut to the city's property tax rate of 19.952 mills.

Improved fiscal health has resulted from improved economic health. The city has experienced marked increases in employment. Detroit, a city whose population is 77.9 percent black, has benefited from an economic expansion that has stretched out to harder-to-reach subsets of the U.S. population. Expanded employment has spurred increases in income—the tax base on which income taxes are levied.

Updated income tax revenue projections exceed what was projected in February. From FY2024 to FY2027, for example, the city is projected to collect $95.7 million more in revenue compared to the February estimate. If the current economic expansion continues in the near-term, the city can anticipate further increases in revenue and some of those additional monies could be returned to citizens as relief from the property tax burden.

To be sure, Detroit has incredible demands on very limited resources, tributes to the past activities—pension contributions and debt service—and the expense of current services to current residents, as well as investments for the future. There is hardly a more imperative need than to halt the near unfettered 70-year decline in population, however. Detroit's property tax rate is far above many other (but not all) jurisdictions, and has been identified as an impediment to development and homeownership. Consider the near quarter of residential structures that have incurred some level of tax delinquency and been ensnared in the foreclosure process that follows. Income tax has been a more substantial source of General Fund revenue relative to property tax, and the city could increase its reliance on income tax to facilitate property tax relief.

Income tax revenue exceeds property tax revenue

Detroit collects revenue from five major sources: income tax, state revenue sharing, wagering tax, property tax and utility users' tax. Based on available audited financial statements, property tax is fourth in the amount of revenue collected. At the September 2023 Revenue Estimating Conference, FY2024 General Fund revenue was estimated at $1.3 billion. Of that amount, $414.7 million (31.9 percent) is income tax revenue, compared to $145.1 million (16.2 percent) in property tax revenue.

From FY2013, the fiscal year that immediately preceded Detroit's descent into bankruptcy, to FY2023, General Fund revenue decreased by 7.9 percent when adjusted for inflation. Over that same period, inflation-adjusted property tax revenue declined by 20.3 percent , the most substantial decline experienced by the five major sources of revenue. Inflation-adjusted income tax revenue, on the other hand, increased by 22.3 percent. While property tax is more stable, it is also relatively less important to the city's financial condition than income tax.

Income tax revenue is projected to increase

Preliminary estimates indicate what was actually collected in FY2023 exceeded expectations from February. Consequently, the city updated its forecast in September to correspond to improved trends. In February, Detroit projected that $1.7 billion would be collected in income tax revenue between FY2024 and FY2027. In September, the city projected it will collect an additional $95.7 million across that same period of FY2024 to FY2027. These additional monies could be used to offset losses incurred from a cut to the property tax rate.

Property taxes are high and a financial burden to low-income residents

Detroit's citizens—many of whom are poor and dispossessed—are subjected to some of the highest property tax rates in the state. Detroit's $34,762 median household income is $18,068 less than the Wayne County median, $28,440 less than the state, and $34,259 less than the U.S. overall. The poverty rate—31.8 percent—is similarly worse than that of Wayne County, the state, and U.S. overall. Part of the reason many of these citizens are dispossessed of their property is because of those high property tax rates. Between 2002 and 2019, an estimated 135,006 properties in Detroit were foreclosed on due to delinquent property taxes. One home in a dataset constructed by Data Driven Detroit was foreclosed on 10 times.

There have been myriad economic improvements in the city. It has experienced lower unemployment rates and higher incomes, but it has not experienced population growth. Detroit is a shrinking city. It is a bitter irony that as the city needs to retain and attract residents, taxpayers, its tax policy likely entices some to leave, and certainly causes some to lose their homes.

Financial stability and service delivery

There are two primary objections to the policy response proposed here: (1) the property tax is more stable than the income tax, and (2) the revenue loss would be detrimental to service delivery. With exception for the Great Recession, which involved a foreclosure crisis and a direct diminution of the tax base upon which property tax is levied, it is less likely to fall in times of economic recession. Between FY2007 and FY2008, income tax declined by 0.7 percent while property tax declined by 15.6 percent. In the brief recession that followed the onset of the COVID-19 pandemic, property tax was comparatively more stable than income tax. Property tax revenue declined by 2.4 percent between FY2019 and FY2020, and income tax revenue declined by 19.7 percent.

There is admittedly short-term risk inherent to more reliance on income tax. The city is prepared for shortfalls in revenue, however. As of the FY2024 operating budget, the city maintains a budget reserve of $150 million, equivalent to 11 percent of General Fund expenditures—this in addition to the ample amount of unrestricted cash the city has accrued since bankruptcy.

In the long term, if the city continues to rely on high property taxes, those high property taxes may be levied on an even smaller economic base. Shifting the tax burden to income from property will lessen a deterrent to development and homeownership. Just as the property tax cannot be solely blamed for the exodus from city borders, property tax relief may not, in and of itself, reverse 70-years of decline, but it will make the city an eminently more attractive place to live and do business.

A second objection, that the revenue loss would be detrimental to service delivery, must also be considered.

Understandably, there is a sense that while services have improved there is more to be done, and the city needs every dollar that flows into the treasury. The size of the city population should be taken into consideration, however. Between FY2013 and FY2023 General Fund expenditures increased by 10.9 percent (when adjusted for inflation), even as population declined by 10.5 percent in that ten-year period.

Today, the city spends more on fewer citizens than it did when it filed for bankruptcy. More to the point, fewer of the dollars expended are spent on pension contributions and debt service. So more resources are directed to service delivery. Yes, labor costs are on the rise, and the current economic moment aside, there is a desire by elected officials to raise police and bus driver pay to parity with nearby jurisdictions. There are and will continue to be substantial demands on city resources. But the city serves fewer residents than decades past and will serve even fewer if population loss continues, as it has, unabated.

Conclusion

The city's property tax has been a persistent problem for development and homeownership. Even as the city makes laudable investments into infrastructure, better pay for essential workers, parks, and beautification, those investments are funded by a policy that directly countervails its efforts to be an attractive place to live, work, and play. The property tax rate could be cut, and incremental income tax revenues may provide the financial cushion to weather the resultant revenue losses.

ABOUT THE AUTHOR

James L. Tatum III - Research Associate, Detroit Bureau

James L. Tatum III is the Researcher for the Detroit Bureau of the Citizens Research Council. Previously, he served as an analyst in the City of Detroit's Office of the Chief Financial Officer (OCFO) where he prepared cost-benefit analyses of City projects, asset sales and labor contracts, forecasted city revenues and expenditures, and conducted scenario analyses for the City's pension plans. In addition to his practical experience, he is an accomplished academic. His research on debt, pensions, insolvency, Chapter 9 bankruptcy, and dissolution has been published in trade, law, and academic journals.

He earned his B.A. in Political Science from Eastern Michigan University in 2014, where he currently lectures, and earned his Master of Public Administration from Syracuse University's Maxwell School of Citizenship and Public Affairs in 2017.

Southeast Michigan
38777 Six Mile Rd. Suite 208, Livonia, MI 48152
(734) 542-8001
Mid Michigan
115 W Allegan St. Suite 480, Lansing, MI 48933
(517) 485-9444
Detroit (313) 572-1840
West Michigan (616) 294-8359