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AN ANALYSIS of the PROPOSED CONSTITUTION

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TAXATION AND EARMARKING OF REVENUES

The proposed constitution includes taxation and earmarking provisions relating both to the state and to local governments. Constitutional provisions on taxation and earmarking of revenues are generally in the nature of limitations on the legislature's power. In the absence of specific state constitutional provisions, the legislature's powers to tax would be relatively unlimited. The provisions of the proposed constitution on taxation and earmarking continue many of the present restrictions on the legislative power, add some new restrictions and eliminate or liberalize some of the present restrictions.

Taxation

Among the major provisions in the taxation section of the proposed constitution are the following:

- The present prohibition against taxation by reference to other tax laws is deleted.
- The present uniform rule of taxation for the general property tax is continued.
- The requirement that all other taxes must be uniform by class is continued. This permits graduated taxes, except for the income tax and the property tax.
- A new explicit restriction is that no income tax may be imposed by the state or its subdivisions that is graduated as to rate or base.
- The four per cent limit on the sales tax is continued.
- The present reference to the 1946 statutory base of the sales tax is deleted, thus clarifying the legislature's authority to define the base.
- The legislature is given greater discretion in determining what kinds of property are to be subject to the general property tax.
- Certain property owned and used by charitable organizations is to be exempt from the property tax.
- Property may not be assessed at more than 50 per cent of the true cash value after Janu-

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- State assessed public service business (utilities) may be taxed at alternate rates.
- The 15-mill limit on property taxes is made less restrictive by providing an alternate 18-mill limit, by exempting taxes levied for debt service, and by specifically exempting from the limitation all charter units of government.
- Only property owners may vote on increasing the millage limitation for more than a five year period.
- Home rule cities and villages and charter counties are given constitutional authority to impose non-property taxes, subject to limitation and prohibition provided by law.

General Provisions

Section 1 of the Finance and Taxation Article (IX) continues the present requirement that the legislature impose taxes sufficient with other resources to pay the expenses of state government. This instruction to the legislature to use its taxing powers to finance the costs of state government is enforced in the proposed constitution by a new requirement that appropriations shall not exceed estimated revenues. The proposed constitution also continues the present prohibition against surrendering, suspending or contracting away the power of taxation.

A significant modification in the general provisions on taxation is the deletion of the present prohibition against tax laws including references to any other law. The new provision requires only that tax laws distinctly state the tax. Thus, under the proposed constitution it would be possible, for example, for a state income tax law to refer to the federal income tax.

There are two other general provisions on taxation that are of considerable significance:

First—Property subject to the general ad valorem property tax shall be taxed uniformly; and,

Second—All other taxes shall be uniform by class.

These provisions continue the present requirements that property taxes be at a uniform rate and upon a uniform base of assessment while all other taxes must be uniform only by class (the rate or base of the tax can vary by class). Thus, taxes other than the property tax can be graduated, with the exception of the income tax (see below).

Provisions Relating to Specified Taxes

In addition to the general provisions on taxation, the proposed constitution contains several provisions relating to specified types of taxes—the income tax, the sales tax, the property tax, and other taxes.

Income Tax. The proposed constitution prohibits the state or any of its subdivisions from imposing an income tax “graduated as to rate or base.” As noted previously, this is an exception to the general provision that taxes other than the property tax may be graduated so long as they are uniform upon the classes upon which they operate. This provision is intended to prohibit a graduated income tax either through progressive rate structure or

through applying a flat rate to a base that is graduated (such as the amount of federal income tax you pay). The convention committee on finance and taxation indicated that this provision would not prohibit allowing reasonable exemptions in a flat-rate income tax, but would prohibit a graduated tax.

Sales Tax. The proposed constitution continues the present prohibition against the legislature imposing a sales tax of more than four per cent on sales of tangible personal property. The present reference in the sales tax provision to the “1946 statutory base (not rate)” has been deleted in order to clarify the legislature’s authority to change the base of the tax. (See below, “Dedication of Revenues,” for the new earmarking provision). The proposed constitution also continues the present provision that the legislature may provide for an excise tax on the retail sales of alcoholic beverages.

Property Tax. The proposed constitution makes a number of changes in the constitutional basis of the property tax and modifies somewhat the present rate limitations.

In respect to the base of the property tax the major provisions and changes are the following:

1. While the present uniform rule of property taxation is continued, it is modified by limiting the rule to “real and tangible personal property not exempt by law.” Under the present constitution all property (including intangible personal property) is subject to the uniformity requirements except property paying specific taxes. Thus, under the present provision property can be exempted from the uniform rule of property taxation only by subjecting it to a specific tax in lieu of the property tax (such as the specific tax on intangibles), while under the new provision property can be exempted by law without imposing any in-lieu tax.
2. In addition, the proposed constitution provides that the legislature may provide for alternate means of taxation of designated real and tangible personal property in lieu of the general property tax.
3. Property owned and occupied by non-profit, religious and educational organizations and used exclusively for their purposes, as defined by law, shall be exempt from the property tax.
4. The legislature is to provide for the determination of the true cash value of property subject to the general ad valorem tax. The uniform assessments of such property shall not exceed 50 per cent of its true cash value after January 1, 1966. This is a major change from the present constitutional requirement that property be assessed at its cash value.
5. The legislature is to provide for a system of equalization of assessments.
6. The legislature is to provide for state assessment of the property of public service businesses now state assessed (telephone companies, railroads, etc.) and of other property designated by the legislature. Property assessed by the state is to be at the same proportion of true cash value as specified for property subject to the general property tax. The proposed constitution provides for alternate rates of taxation on such property: 1) the average state tax rate on general property (total state equalized value of property divided by the total amount of general property taxes levied) presently used, or, 2) the legislature may provide as an alternate that the property of each business assessed by the state be taxed at the average rate of those counties in which the prop-

erty of the business is situated (total state equalized value in counties in which property is located divided by the total general property tax levy in those counties).

In addition to the provisions on the base of the property tax and the method of taxing the property of public utilities, the proposed constitution also contains several provisions limiting the rate of the property tax:

1. While the 15-mill limit on property taxes is continued, an alternate 18-mill limitation is provided. Under the present and proposed 15-mill limitation the 15 mills must be allocated among the units subject to the limitation. Under present law this is done annually by a tax allocation board in each county. The proposed constitution provides that under procedures provided by law a majority of voters in any county may approve separate tax limitations for the county, and the townships and school districts therein, which limitations cannot exceed an aggregate of 18 mills. This separate tax limitation provision would eliminate the necessity for annually allocating millage among the various units. The separate rates may be changed by vote of the people, but the total cannot exceed 18 mills.
2. Taxes levied for the payment of principal and interest on bonds are specifically exempted from the millage limitations and may be levied without limitation as to rate or amount. Thus, approval of a bond issue will automatically carry with it authorization to levy the taxes necessary to retire the debt.
3. The 15-mill or 18-mill limitation may be increased to an aggregate of 50 mills for not more than 20 years at any one time, if approved by a majority of the *qualified* electors voting on the question. Under the Elections Article (II) of the proposed constitution only property owners and their spouses are qualified to vote on an increase for a period of more than five years. At present any elector can vote on a millage increase.
4. Specifically exempted from the millage limitations are cities, villages, charter counties, charter townships, charter authorities or other authorities, whose tax limitations are provided by charter or by general law. The general laws providing for city and village home rule and charter counties shall limit their rate of ad valorem property taxation.
5. The new provision specifically applies the limitation to the “assessed valuation of property as finally equalized,” which is the current practice by court interpretation.
6. A new proviso is that the property tax limit in any school district extending into two or more counties may be that available in the county containing the greatest part of the area of the district.
7. The proposed constitution continues the present provision that the general property tax for county road purposes cannot exceed in any year one-half of **one** per cent (5 mills) of the assessed valuation for the preceding year.

Local Non-Property Taxes. A major innovation in the proposed constitution is the authorization for home rule cities and villages and charter counties to levy non-property taxes, subject to constitutional and statutory limitations and prohibitions. These local units will thus have considerable discretion in imposing taxes while the legislature will be able to regulate the non-property tax field by prohibiting or limiting specified kinds of non-property taxes. At present, all constitutional taxing authority is vested in the state, and local units can levy only those taxes which they are authorized to levy by the state.

Present laws authorize counties to levy only the property tax and home rule cities and villages can levy only the property tax and “excises” if so provided in their charters.¹

Earmarking of Revenues

Among the tax revenues presently earmarked or dedicated to expenditures for particular purposes by constitutional provisions are the gas and other motor vehicle taxes, two and one-half cents of the four cent sales tax, and a number of specific taxes earmarked to the primary school interest fund. The proposed constitution continues the earmarking of gas and motor vehicle taxes and the sales tax, but eliminates the earmarking of specific taxes to the primary school interest fund.

Highway User Taxes

The proposed constitution continues the earmarking for highway purposes of taxes on motor vehicle fuels and motor vehicles but adds a new provision that “highway purposes” are to be defined by law. This will place primary responsibility in the legislature for determining what constitutes a highway purpose for which the earmarked funds may be expended. The new provision omits much of the detail in the present constitution.

Sales Tax

The present four per cent limit on the sales tax and the earmarking of a sizeable portion of sales tax revenue for local units and schools are continued.

Under the present provision one-half cent of the sales tax is to be returned to cities, villages, and townships on a per capita basis and two cents is earmarked to the school aid fund for aid to school districts. The proposed constitution makes several changes in the earmarking to local units and school districts.

Local Units

1. Instead of earmarking one-half cent of the sales tax, the proposed constitution earmarks one-eighth of the total retail sales tax. While under the present four per cent levy this amounts to the same thing, the use of a fixed proportion (one-eighth) instead of a fixed rate (one-half cent) will provide for an adjustment in the amount returned to local units if the rate of the sales tax is changed.
2. The new provision deletes the present reference to the “1946 statutory base (not rate)” thus clarifying the legislature’s authority to change the base of the sales tax and to revise accordingly the amount of earmarked revenues. Thus, under the proposed constitution the legislature could exempt some class of sales from the tax and the resulting revenue loss would be reflected in the distribution to local units and schools.
3. While the new provision continues to require distribution to cities, villages and townships on a population basis, the present detailed computation procedure is deleted and the distribution is to be as provided by law.

¹ The question of whether a local income tax is an “excise” within the meaning of the home rule act is now before the Michigan Supreme Court.

School Aid

1. The proposed constitution earmarks one-half of the sales tax revenue (instead of two cents) and “other tax revenues provided by law” to the school aid fund. As in the case of local units, the use of a proportion (one-half) instead of a fixed rate (two cents) will permit increases or decreases in the sales tax revenues earmarked for schools if the total state rate is changed.
2. The present reference to the 1946 statutory base is omitted also from the school earmarking provision.
3. The present provision limits use of these earmarked funds to aid to school districts and school employees retirement systems, providing that there shall be appropriated to the retirement systems not less than 5 per cent nor more than 7.5 per cent of the salaries of the school district employees participating in the retirement systems. This provision is modified in the proposed constitution by providing that the school aid fund be used for aid to school districts, *higher education* and school employees retirement systems. “Higher education” is added to the list of purposes for which the earmarked funds may be used and the provision on the amount to be appropriated to the retirement systems has been deleted.

One further change should be noted—under the present provision earmarking sales tax revenues to local units and schools the cost of collection of the tax is deducted prior to distribution. Thus, the amount distributed is *net* after collection costs. The proposed constitution deletes this reference to deducting collection costs. Thus, apparently one-half and one-eighth of the *total* sales tax collection will be returned to schools and local units respectively, with the cost of collection borne by the general fund of the state.

Other Earmarking

The proposed constitution does not continue the earmarking of taxes to the primary school interest fund. The present constitution establishes a primary school interest fund and dedicated the inheritance tax, foreign insurance company taxes, and the ad valorem taxes on railroads, telephone and telegraph companies, etc., to that fund. Inasmuch as the primary school interest fund monies, currently about \$62 million a year, are now used as an offset in the school aid fund distribution formula, elimination of the provision will not reduce automatically state aid to local schools. However, elimination of the constitutional earmarking will increase legislative discretion in this area. It should be noted also that the new school aid fund provision authorizes “other tax revenues provided by law” to be dedicated to the fund in addition to the one-half of the sales tax.

In addition to these provisions earmarking tax revenues, the proposed constitution continues the earmarking of penal law fines to the support of libraries, adding that county law libraries may also be supported from such fines.