



# Ongoing Financial Troubles of Michigan's Local Governments

Leadership Summit  
April 14, 2011

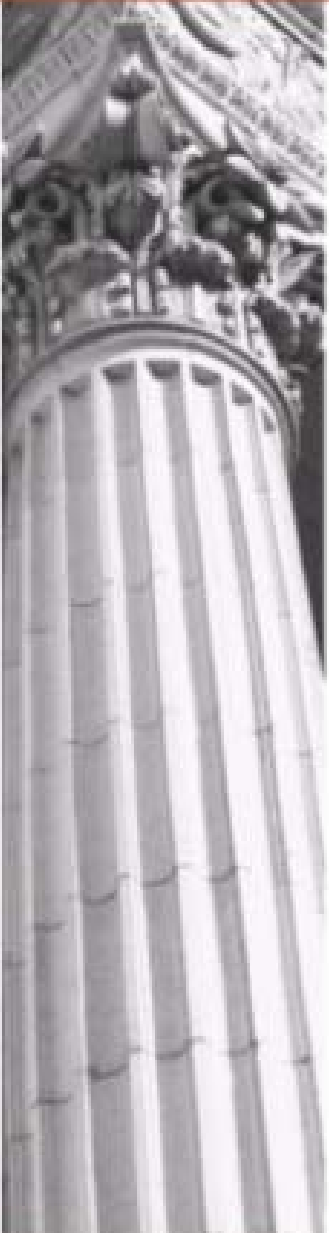
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## Citizens Research Council of Michigan

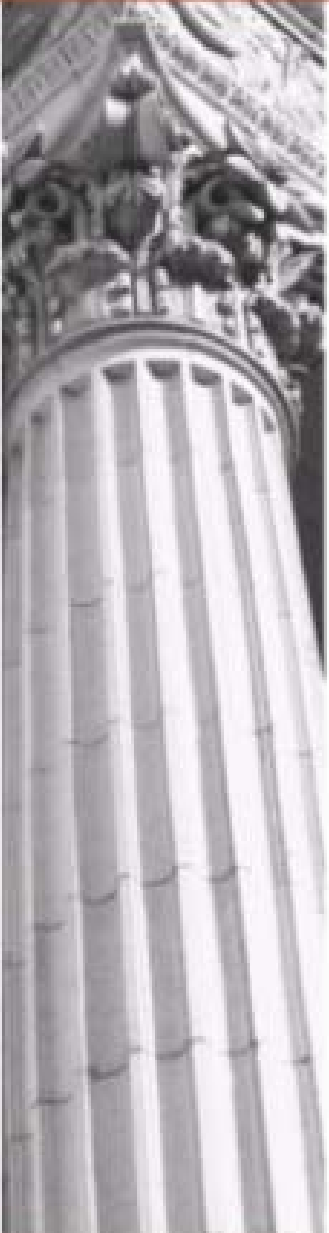
- Founded in 1916
- Statewide
- Nonpartisan
- Private not-for-profit
- Promotes sound policy for state and local governments through factual research
- Relies on charitable contributions from Michigan foundations, businesses, organizations, and individuals





## Recent Headlines

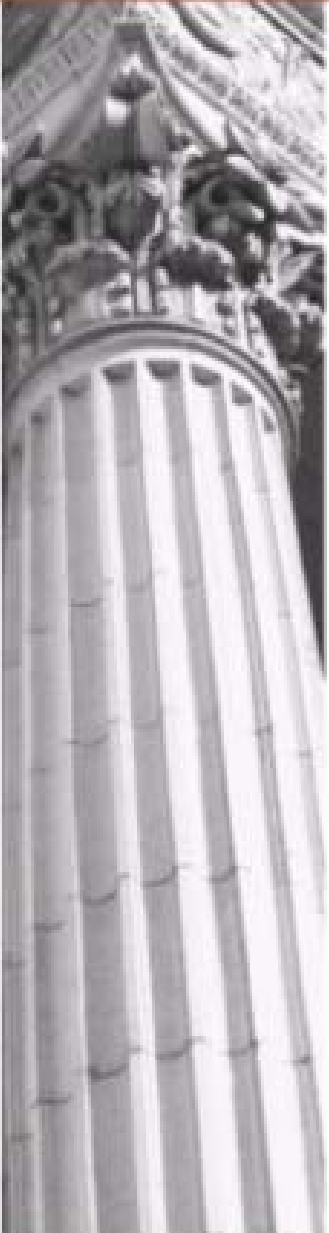
- Michigan communities struggle with budget cuts
- Tecumseh looks at reducing some city services
- East Lansing cuts \$1.9 million from city budget
- Grand Rapids city manager says budget cuts may force layoffs, City Hall closure for two weeks
- Cuts may eliminate 41 Grand Traverse County jobs
- Negaunee council looking for more cuts to budget





## Still Early-Mid Stages of Local Government Recession

- Property tax bases continue to decline for several years
- Property tax bases recover at snails pace when real estate markets recover
- Little prospect of state fully funding statutory state revenue sharing
- Local government will continue to shrink





## Local Government Revenue Sources

- Property Taxes
- State Revenue Sharing
- Income Taxes
- Federal Funds





## Property Tax Base Growth

### For Local Governments

- Average 7% annual growth in tax base
- Little year-to-year fluctuation

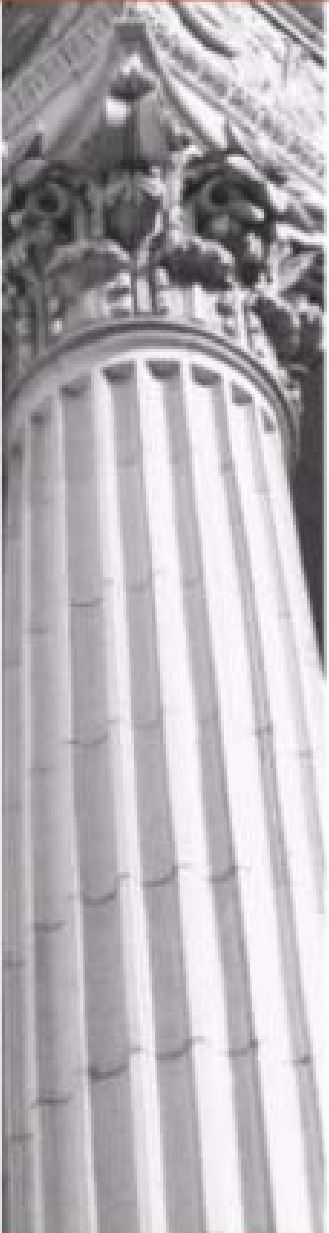
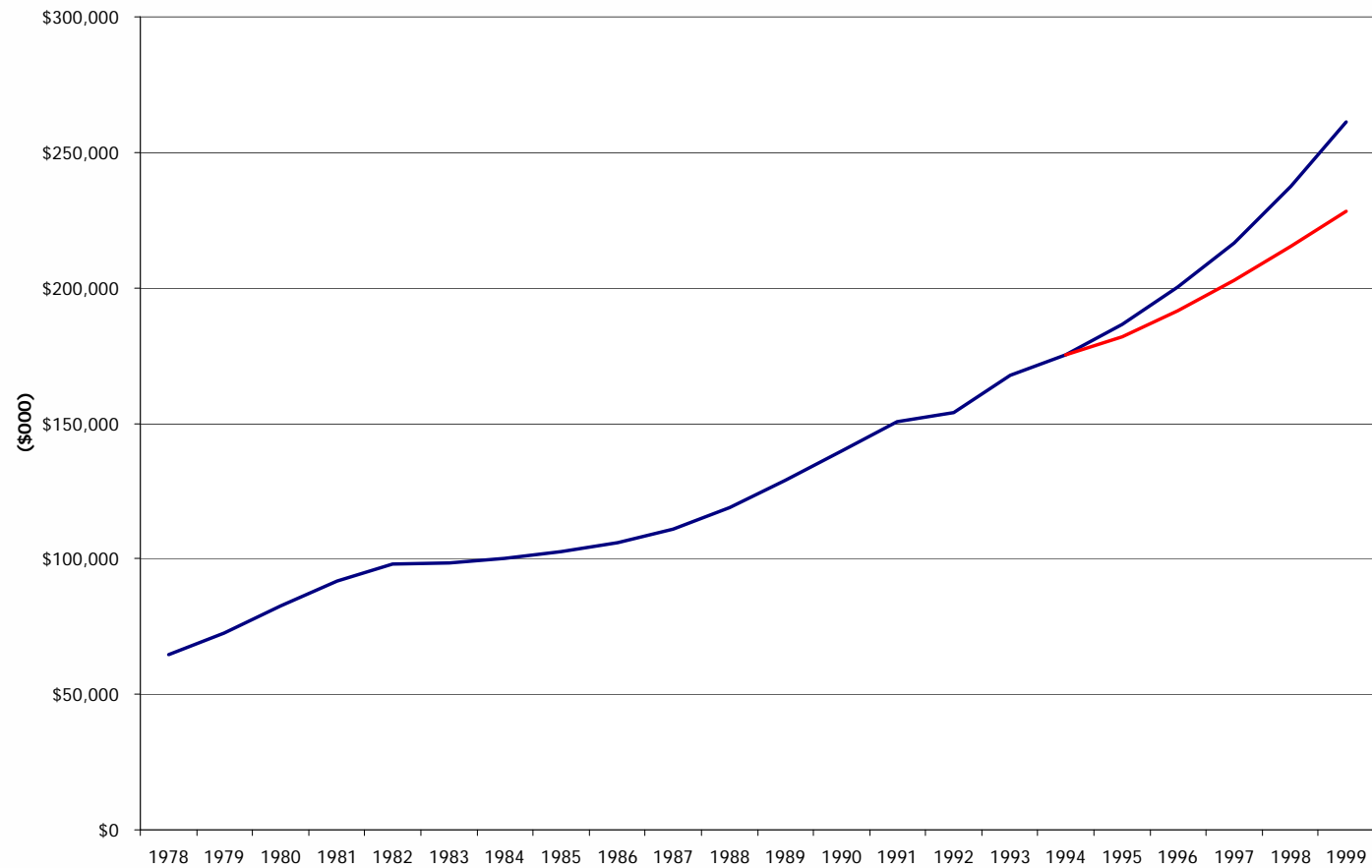
### For Property Owners

- Increasing tax burden even when ability to pay decreasing
- Growth in tax base often outpaced inflation





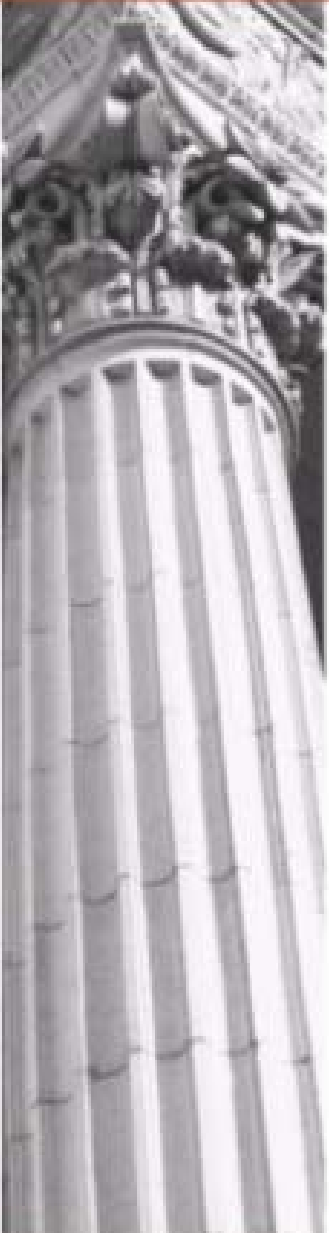
## Steady, Consistent Growth of Property Tax Base





## Taxpayer's Response to Steady Consistent Growth of Tax Base

- Headlee Amendment
  - Unit-wide cap on growth of tax base
  - Rate of inflation
  - Tax rate "rolled back" so net yield = inflationary growth
  - Individual parcels could still grow faster than inflation
  - New development helped keep government revenues strong

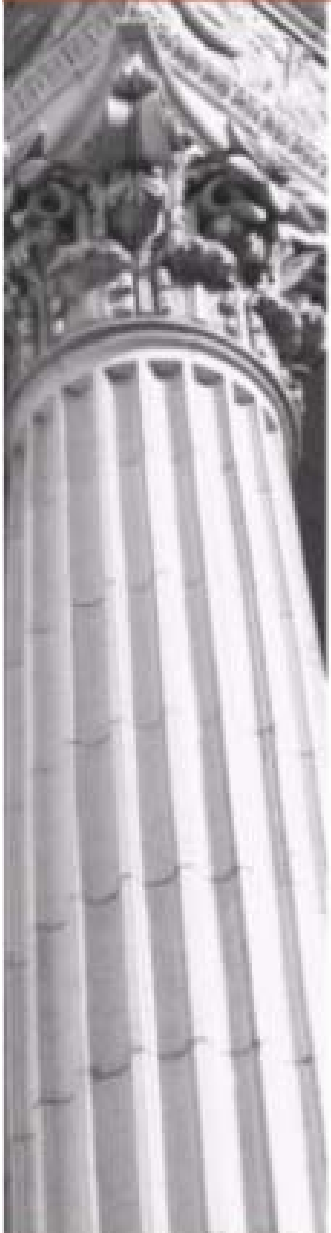


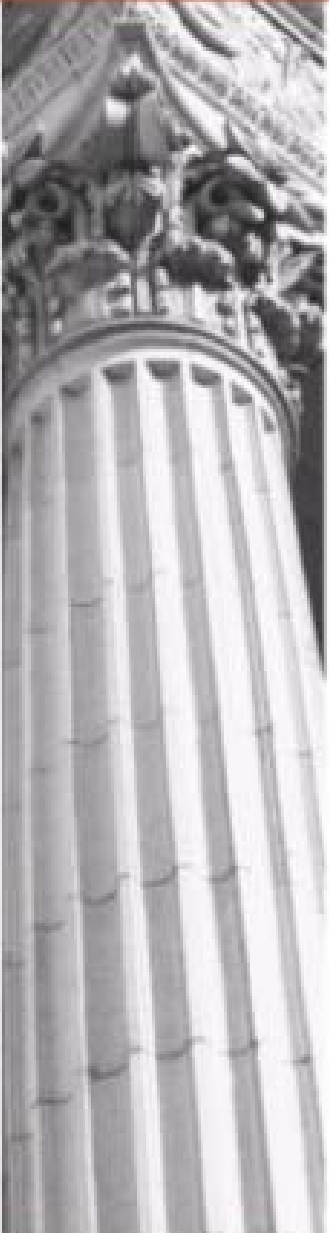




## Taxpayer's Response to Steady Consistent Growth of Tax Base

- Proposal A of 1994
  - Limit growth of individual parcels to rate of inflation
  - Return to SEV when ownership transfers
  - New development helped keep government revenues strong
  - Ownership transfers caused unit-wide growth to trigger Headlee tax rate rollbacks



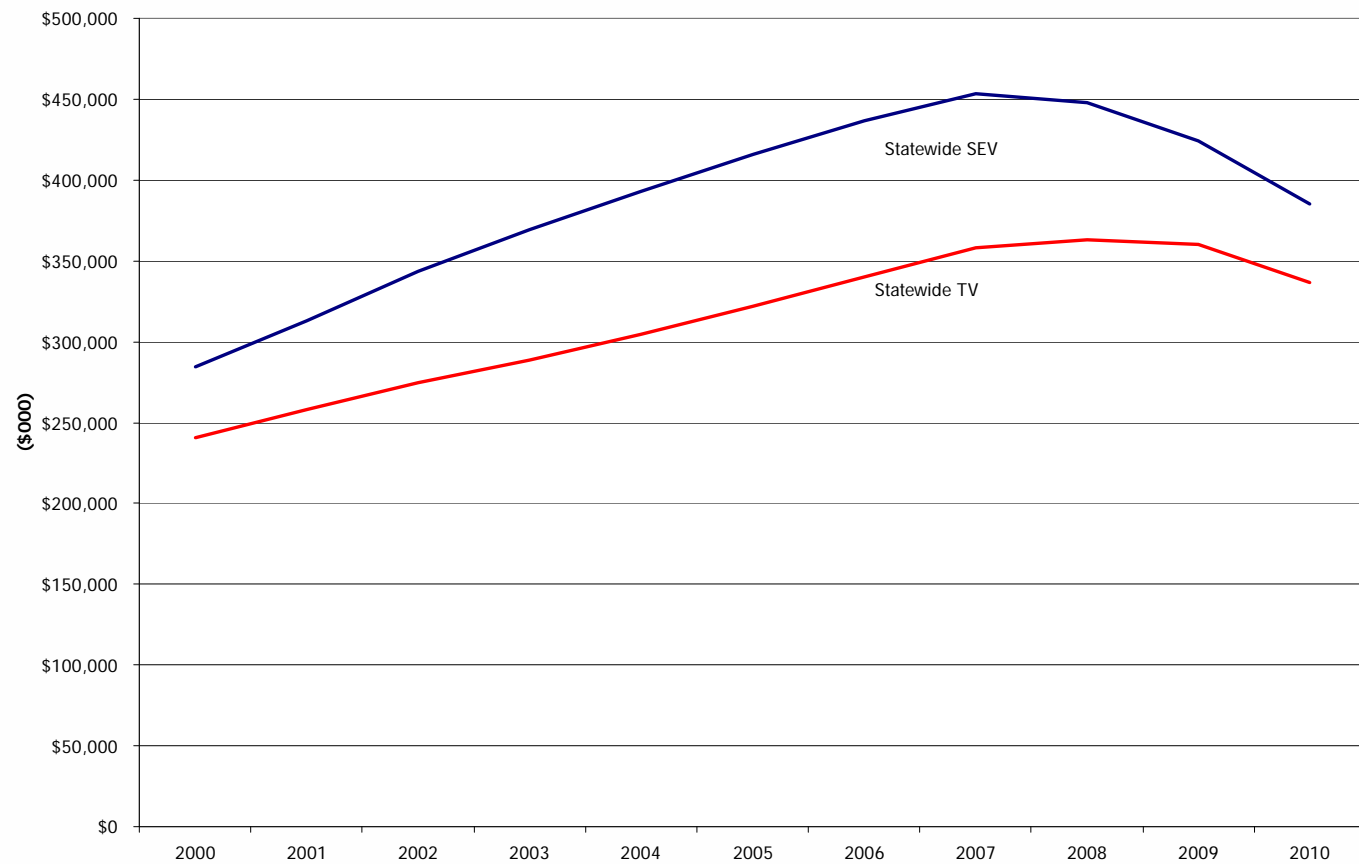


## What Happened?

- Decline in manufacturing and automotive sector employment
- Housing bubble popped nationwide
- Real estate collapse became a major contributor to recession
- Foreclosures became a problem
  - Particularly in SE Michigan
- Demand for second homes declined
  - Particularly hurting northern Michigan



## Reversal of Fortune in 2000s





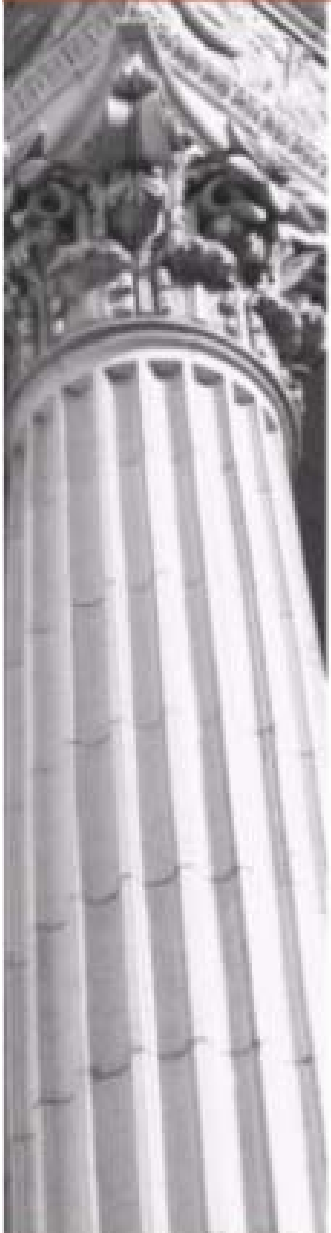
## When will Tax Base Recover?

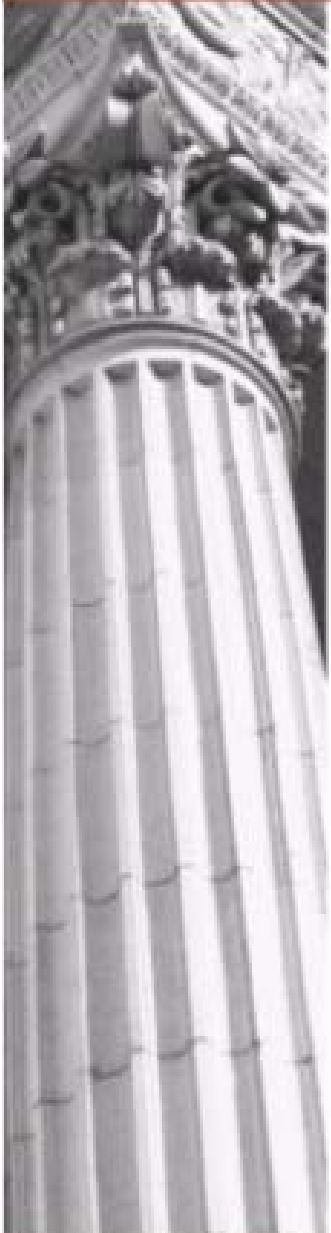
- Still a number of unknowns that will influence the answer to this question
- When will residential decline carry over to commercial and industrial properties?
  - Record number of appeals in MTT
- When will state become attractive place for new development?
  - End population exodus
  - Exhaust surplus of housing stock



## Lag in Government Reflecting Economic Change

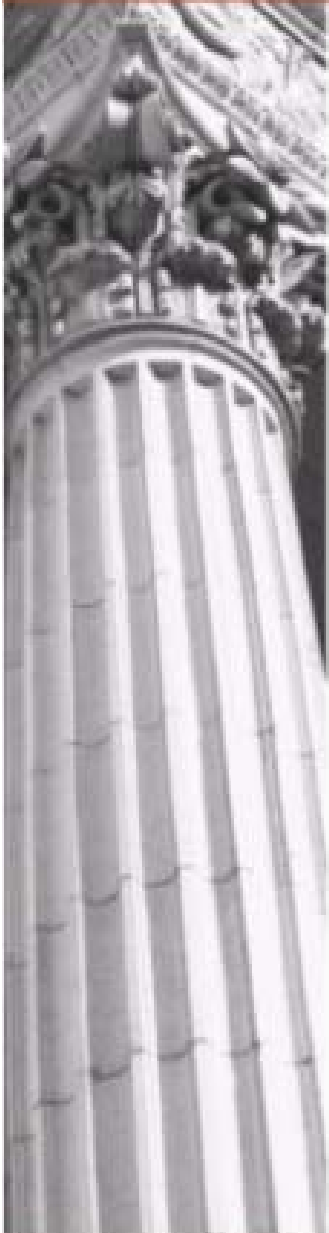
- Delayed impact of private sector recession on local government tax bases
  - 3-5 year lag on property tax bases
  - Usually on both sides of a recession, but it will be longer this time for Michigan because of "Taxable Value"
  - 2023-27 before tax bases return to 2007 levels
- Governments receive revenue in regular intervals
  - State – monthly for most taxes
  - Local – 2x/year for property taxes



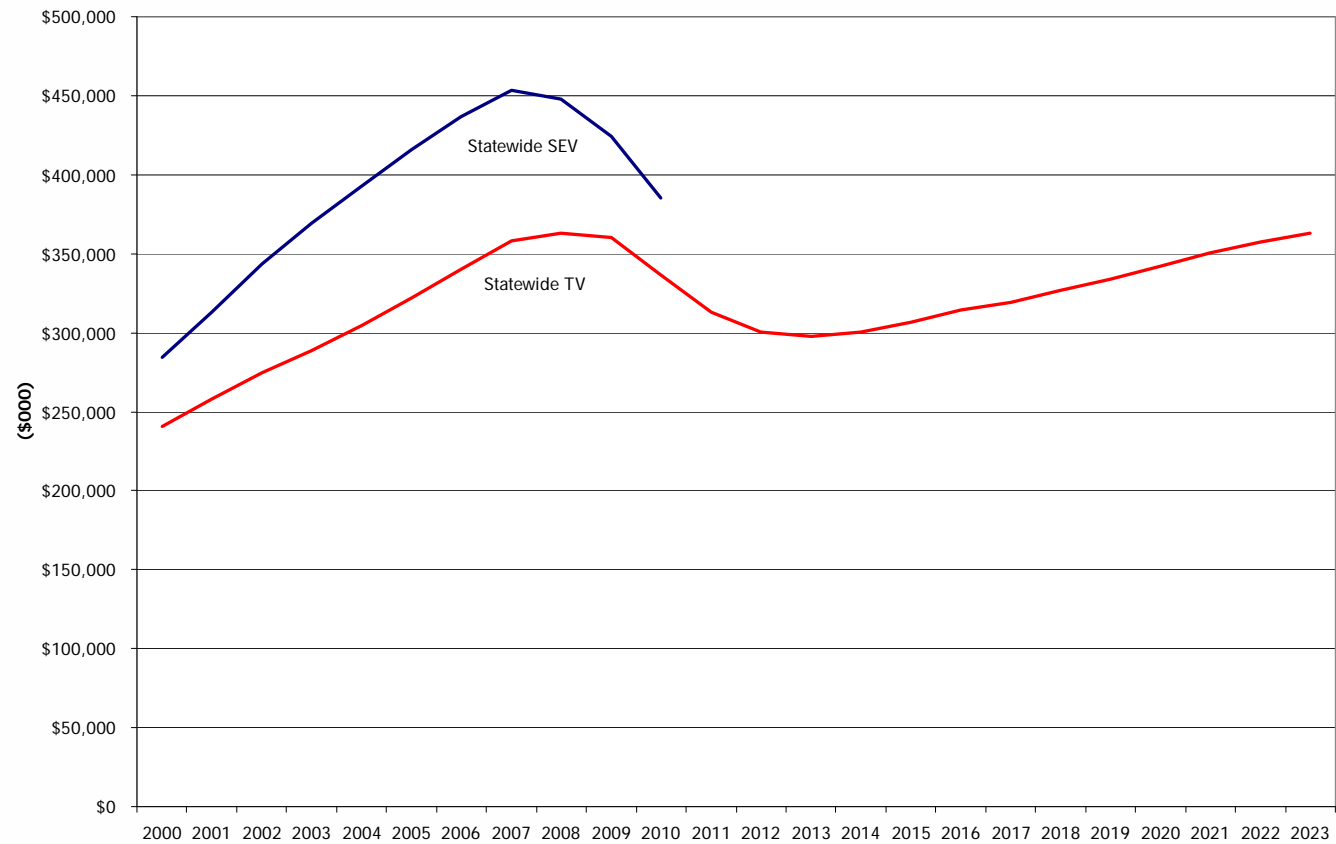


## Repercussions

- A lot of people “trapped” in their current homes
  - Without benefit of appreciated value they don’t have money to put down for housing upgrades
- Tax capture for TIF funding greatly impacted
  - TIF, DDA, LDFA, Brownfield districts with little growth relative to base year
- Infrastructure installed for developments that didn’t occur
  - Good chance of bond defaults because of project decisions made during good times



# Prolonged Recovery

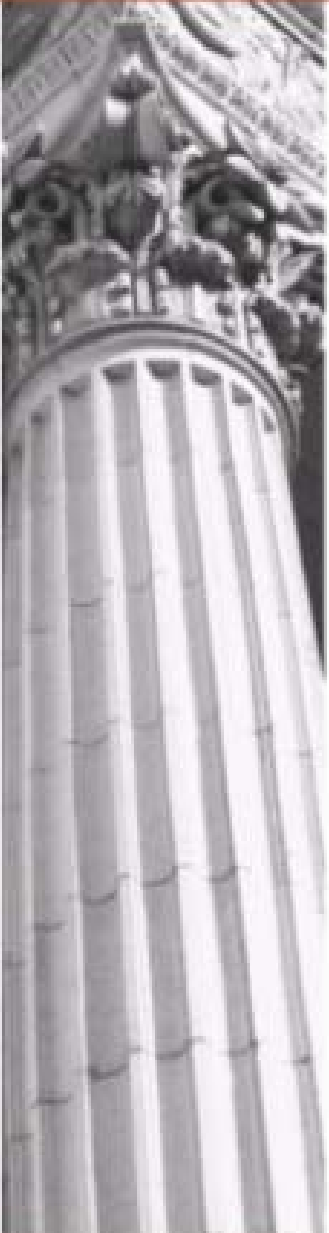




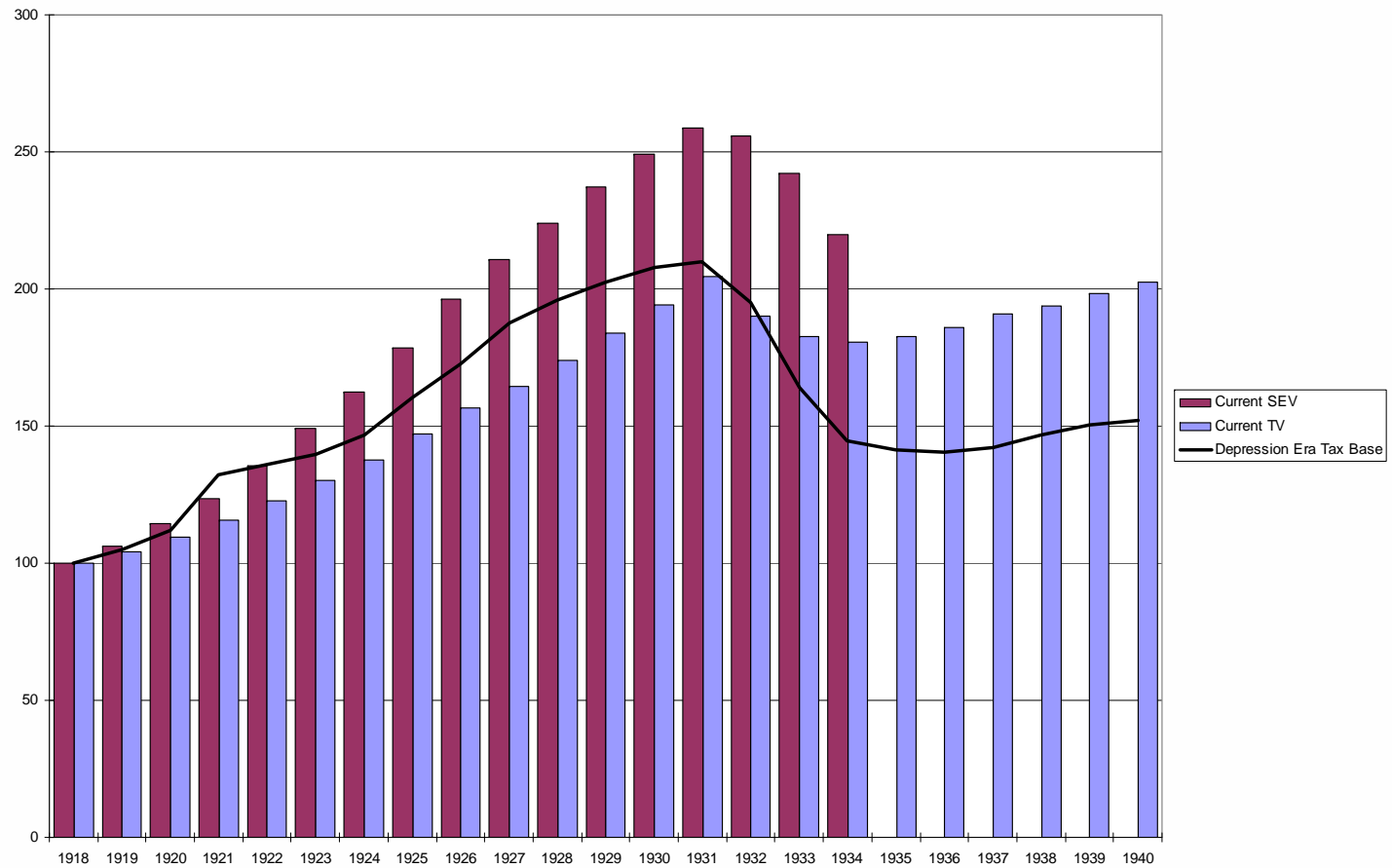
## The Big Picture

- A few more years of declining tax base
- Statewide Taxable Value down about 20% by 2013
  - More in some regions, less in others
- Weak growth in real estate markets and property tax limitations collude to cause restrained growth in tax base
- Use of Taxable Value means decline will be only  $\sim \frac{1}{2}$  of that experienced in Great Depression





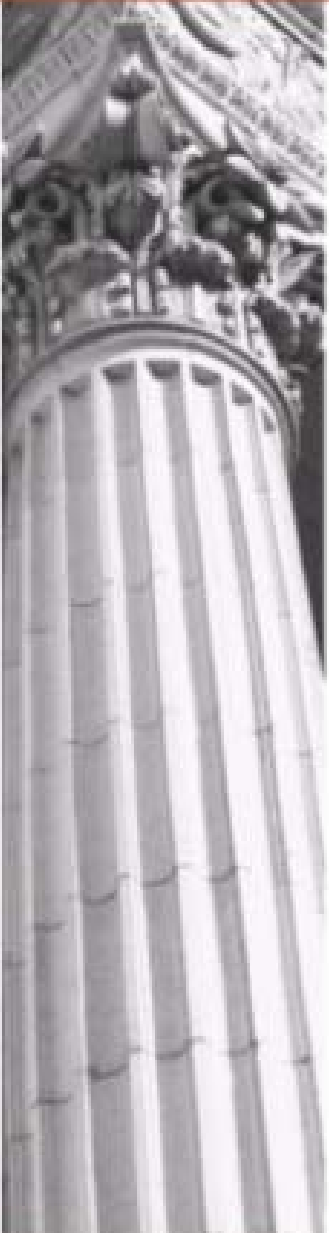
## It could be worse!





## State Revenue Sharing

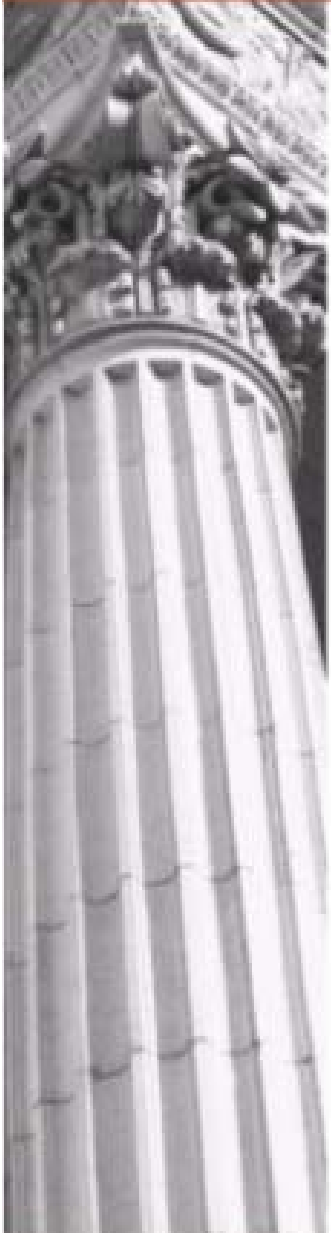
- Constitutional Program – Article IX, Section 10 of MI Constitution
  - 15% of 4% Sales Tax distributed on a per capita basis to townships, cities, and villages
  - All 1800+ CVTs receive this funding
- Statutory Revenue Sharing – Weighted formula used since 1971 (1998 in its current form)
  - Only about 700 cities and charter townships receive this funding





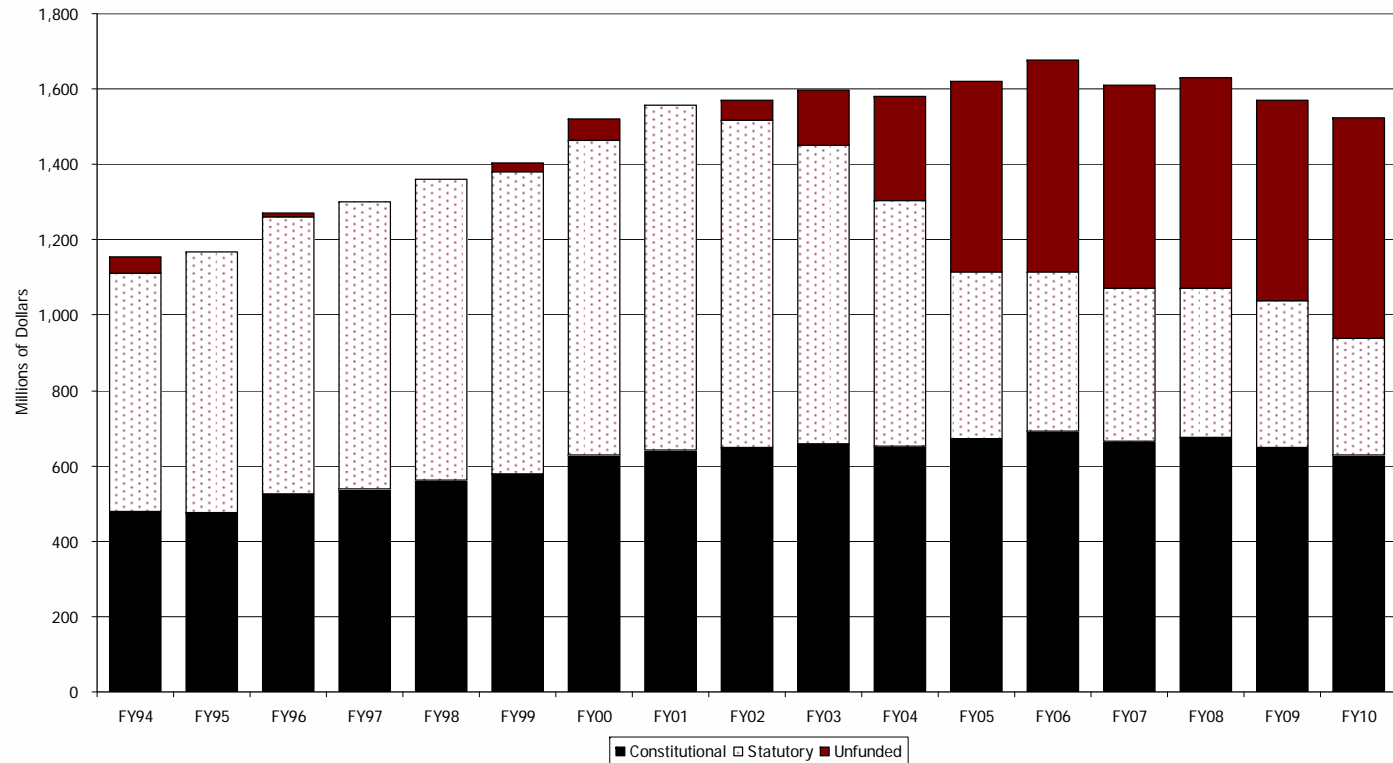
## **Diversions for Other State Purposes**

- Diversions started in 2001
- Total of \$4 billion has used by state for other purposes
- Decline or hold constant while sales tax revenues growing caused constitutional revenue sharing to grow at expense of statutory revenue sharing
- Only about 700 cities and charter townships still receive funding





## Actual & Foregone State Revenue Sharing





## State Revenue Sharing

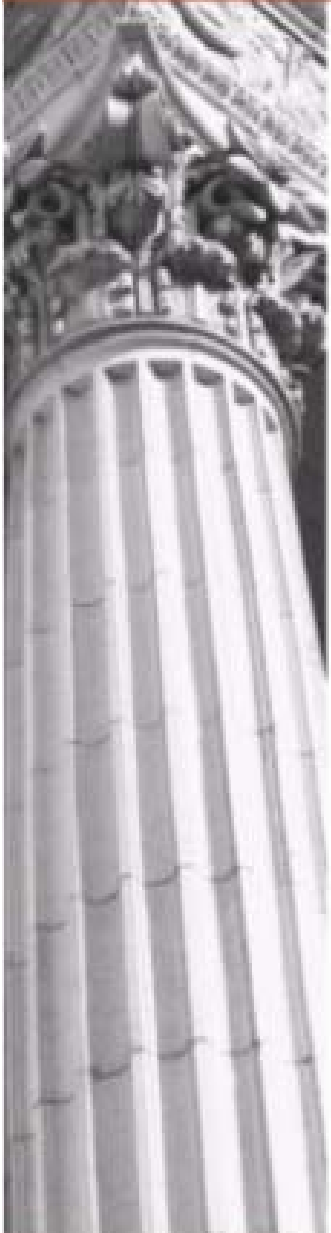
- Why Bother? Isn't this just a program for the state to send money to local governments when it has enough?
- Enhance Tax Equity – broader geographic area
- Minimize Market Disruptions – multiple taxing entities with varying tax rates lead people to alter market decisions to avoid taxation





## Why State Revenue Sharing?

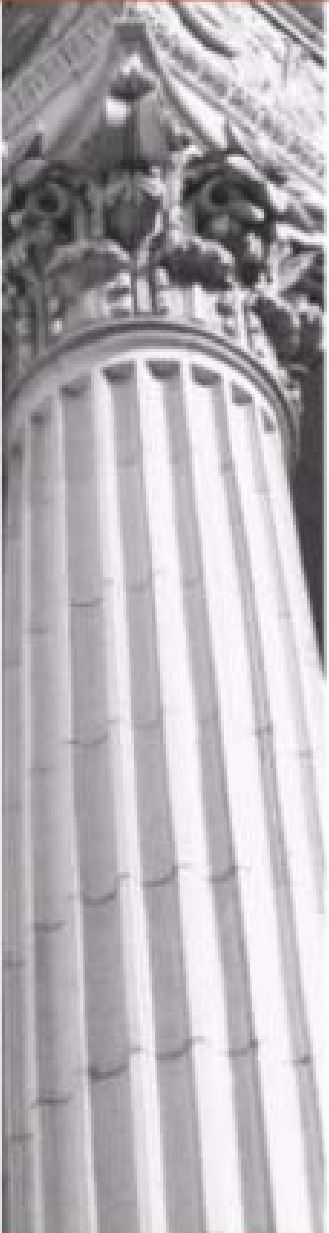
- Tax Base Diversity – diversify tax base beyond property tax
- Property Tax Relief – alternative revenue sources allow for lower property tax rates
- Enhance Taxpayer Efficiency – easier to interact with a single collecting agency
- Service Maintenance – State taxes preempted local taxes
- Minimum Level of Services – equalize the revenue raising capacity of local governments





## Income Taxes

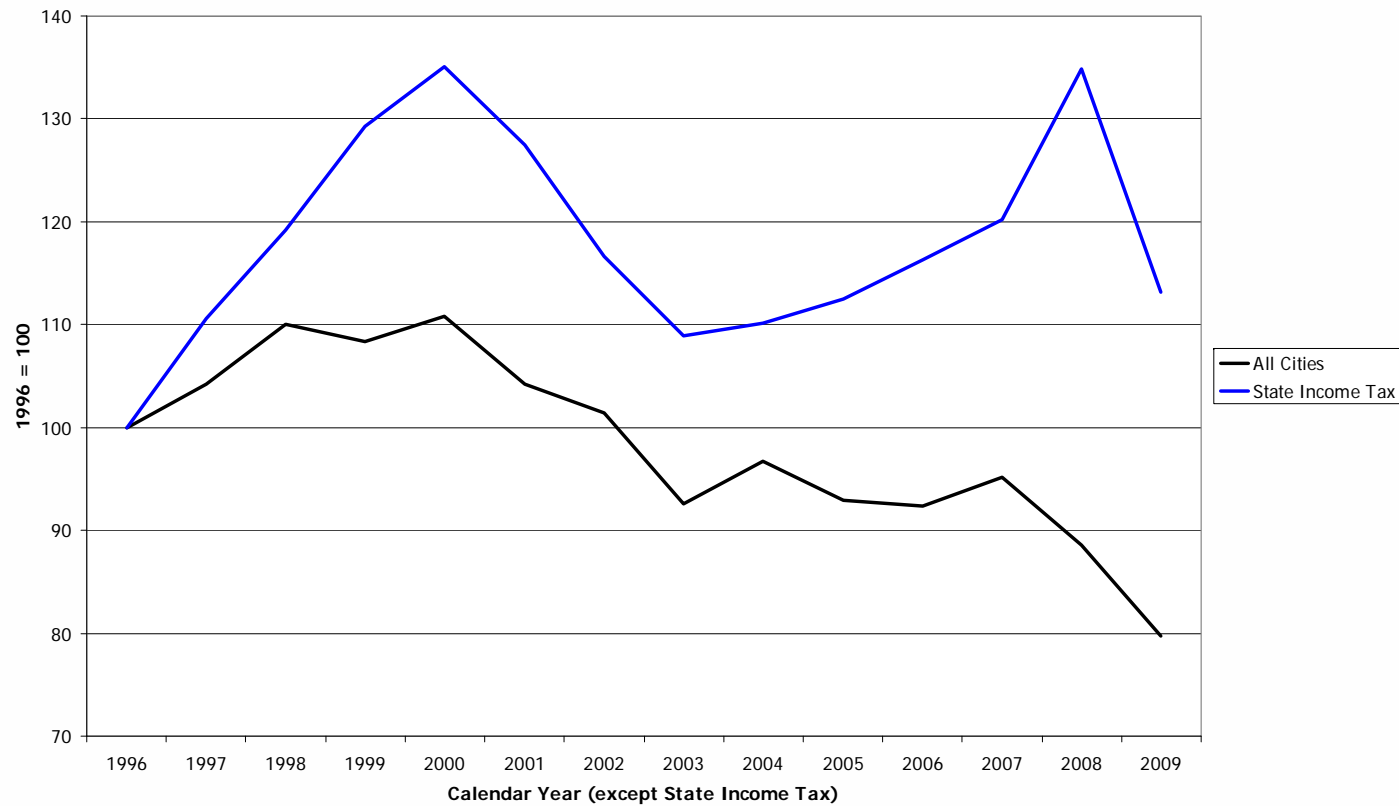
- Only available to Michigan cities
  - 22 cities actually levy
- Results have been mixed
  - Less productive than property taxes
  - Productive supplement to property taxes for smaller Michigan cities
  - Bigger cities have seen revenue growth at slower rates than state income tax





# State vs City Income Tax Revenues, 1996 - 2009

Revenue Trends for Michigan City Income Tax Revenues

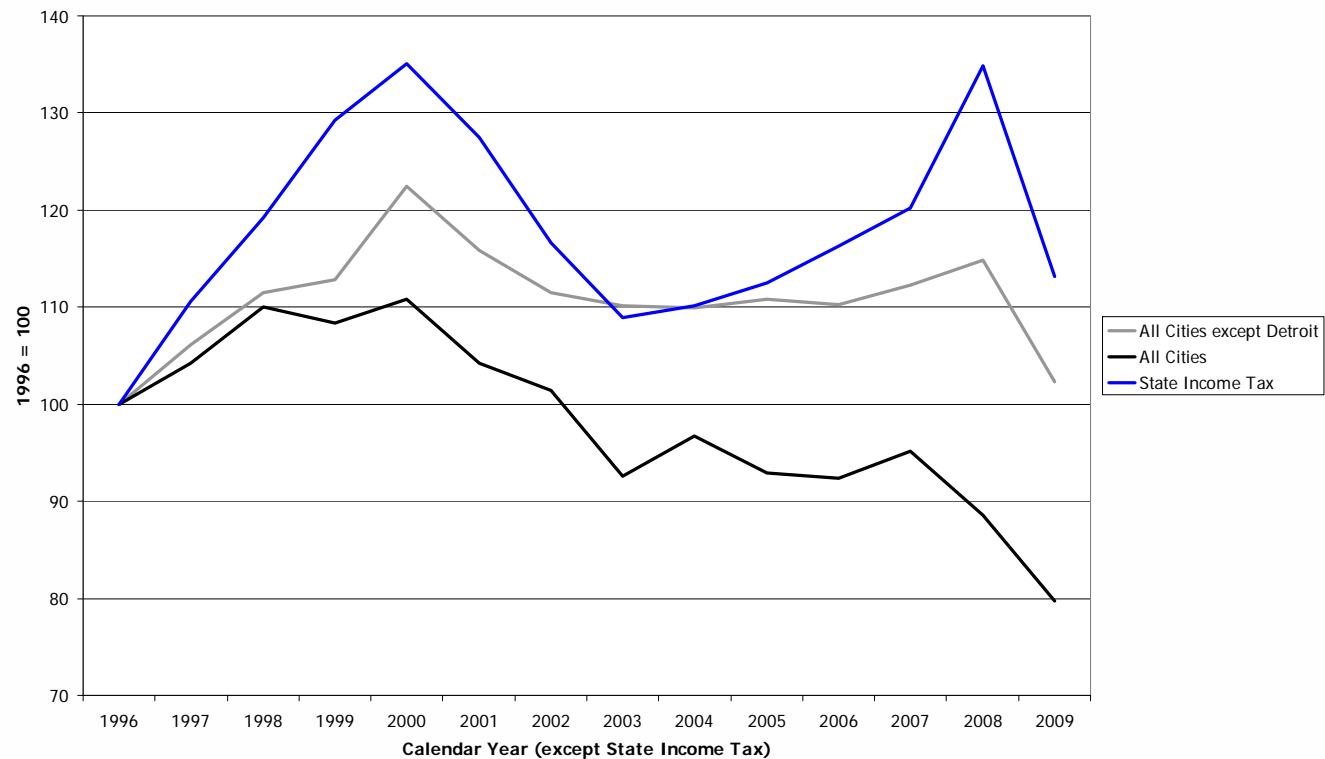






# State vs City Income Tax Revenues (without Detroit)

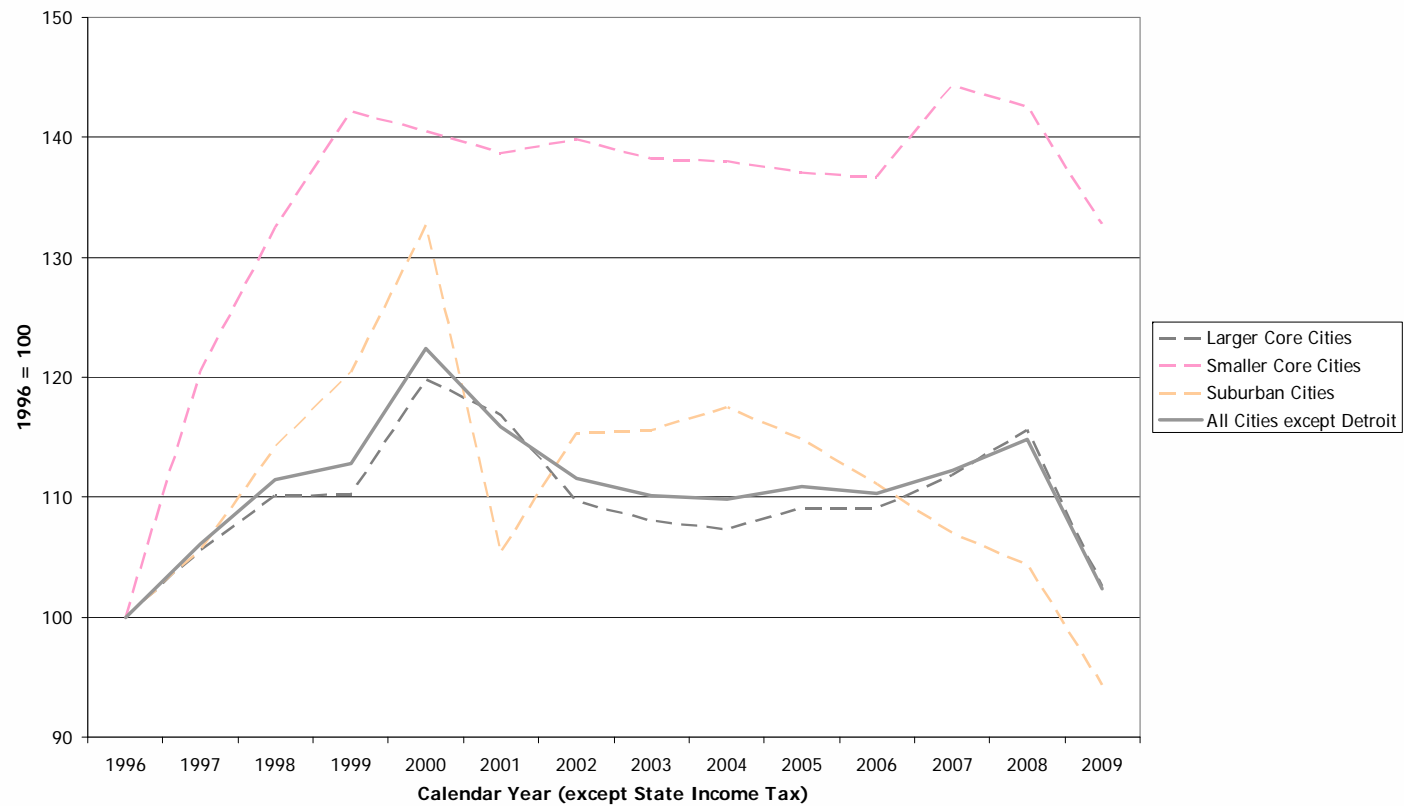
Revenue Trends for Michigan City Income Tax Revenues





## Different Experiences for Different Size Cities

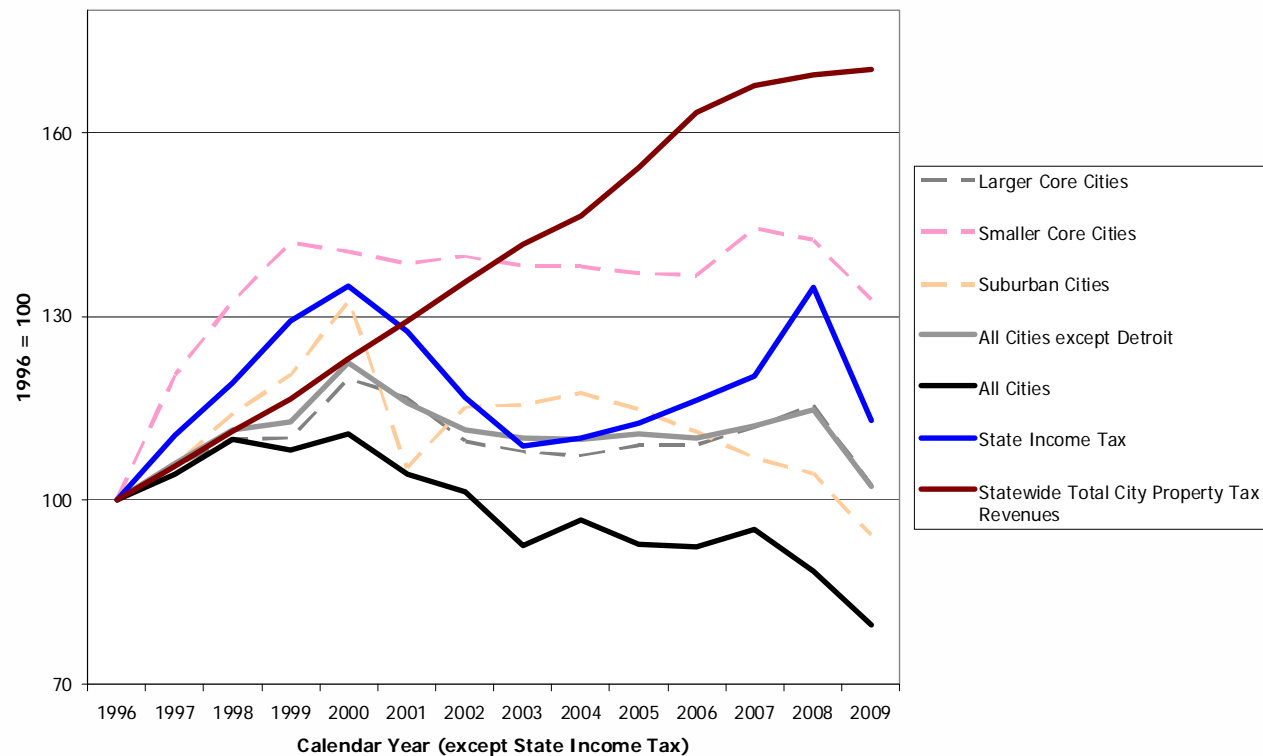
Revenue Trends for Michigan City Income Tax Revenues





## Still would have been better off with the property tax

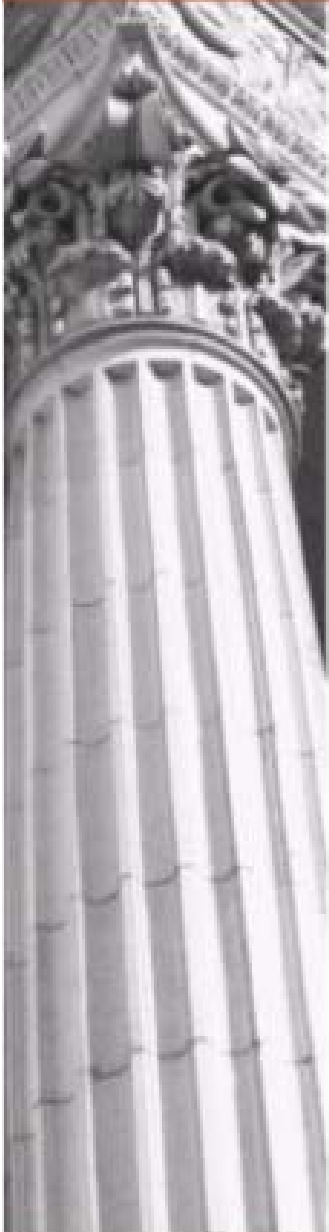
Revenue Trends for Michigan City Income Tax Revenues





## Federal Funds

- **Unlike state government and school district, ARRA funds for local governments never supplemented operations**
- **Overall federal funding to cities down 50% over last 5 years**
- **CDBG funding in danger with Obama and Republicans wrangling over federal budget**



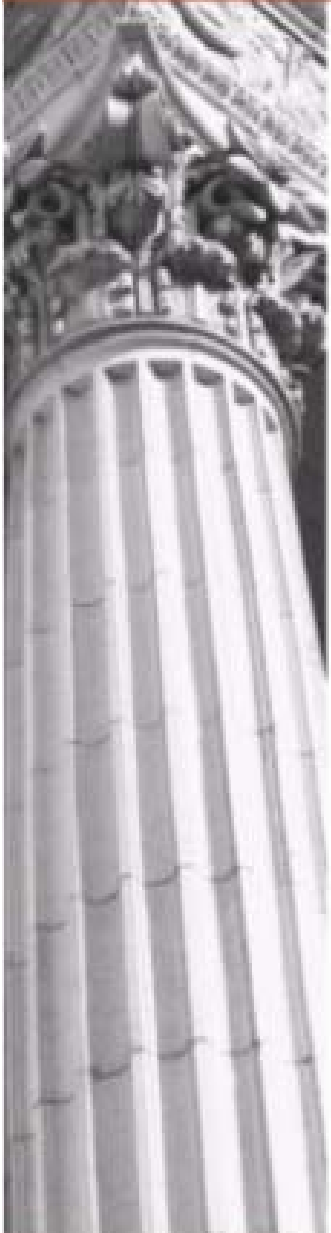
## How to Respond to Recession

- **Business** – supply and demand
  - Production adjusted to meet changing demand
- **State Government** – program/department spending pressures driven by independent variables
  - e.g., population in poverty, number of incarcerations, university / school age children
- Some variance with economic cycles
- Some spending designed to be counter-cyclical
  - e.g., Medicaid, unemployment insurance, workforce training



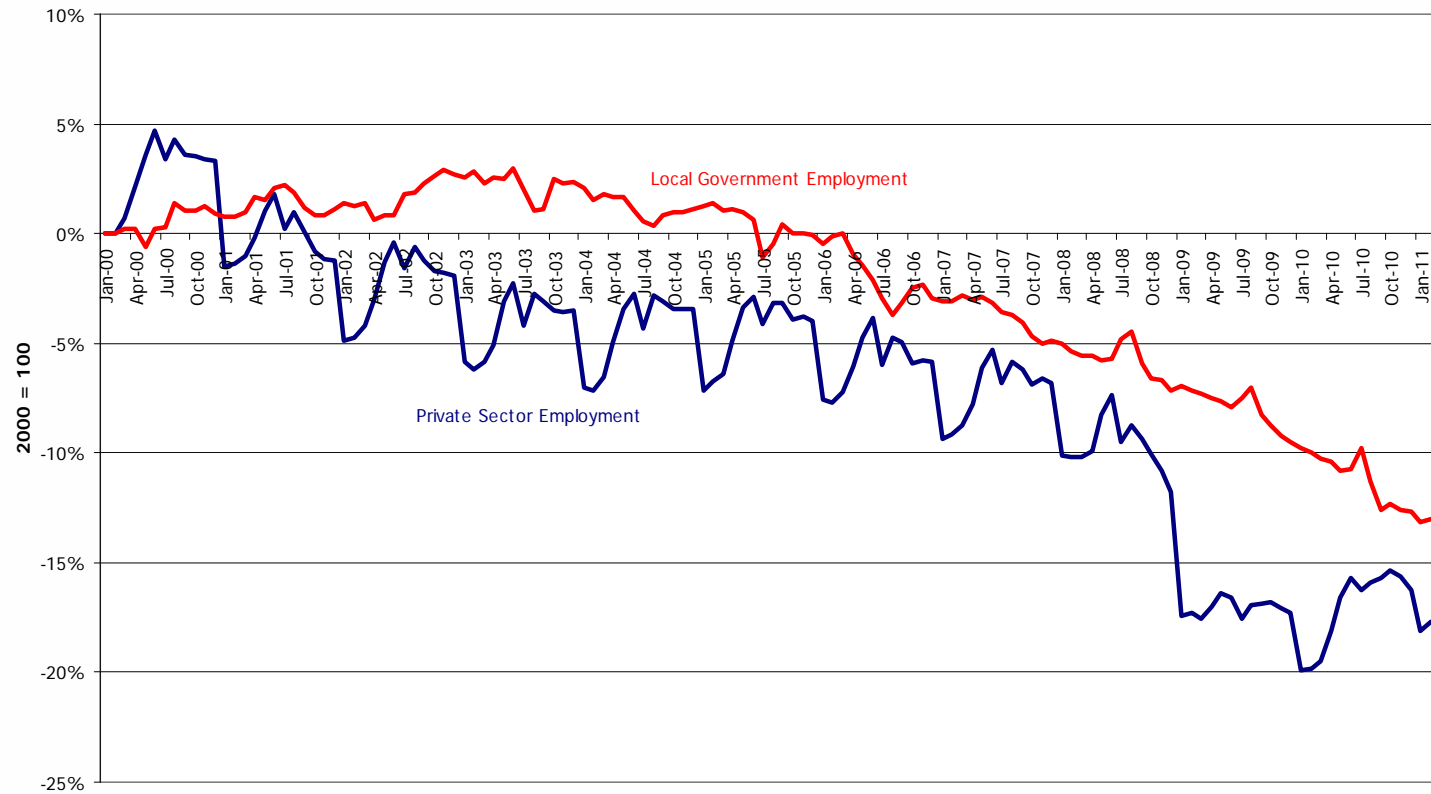
## How do Local Governments Respond?

- Most determining variables experience little year-to-year fluctuation
  - Number of square miles – fire protection
  - Number of street miles – police patrol
  - Number of parcels – garbage collection, fire protection
  - Population – use of senior center, parks and recreation programs
- Little variation because of economic fluctuations
  - Exceptions – county health, tourist towns



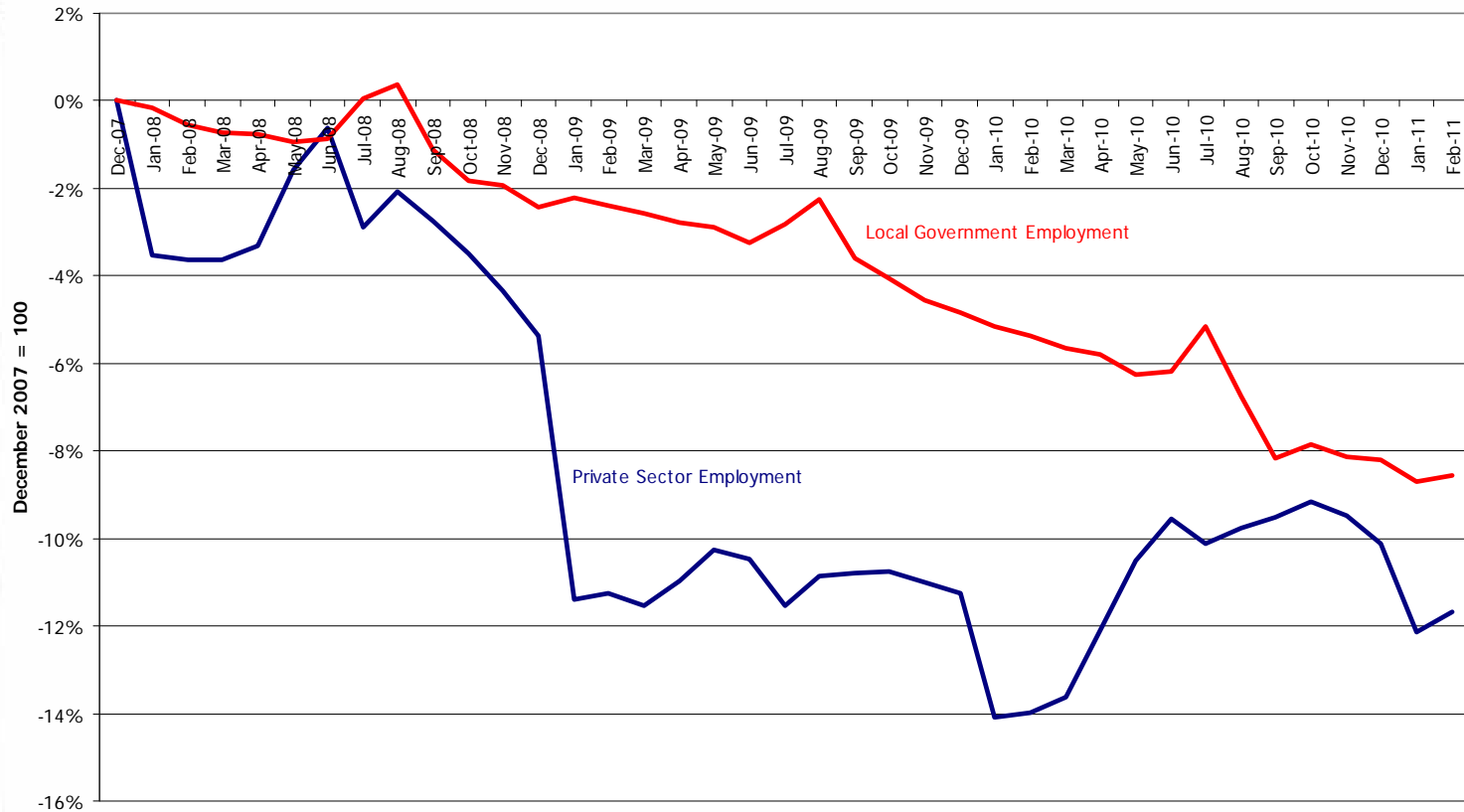


## Local Government Response to Date – Downsize





## Local Government Response to Date – Downsize (pt. 2)

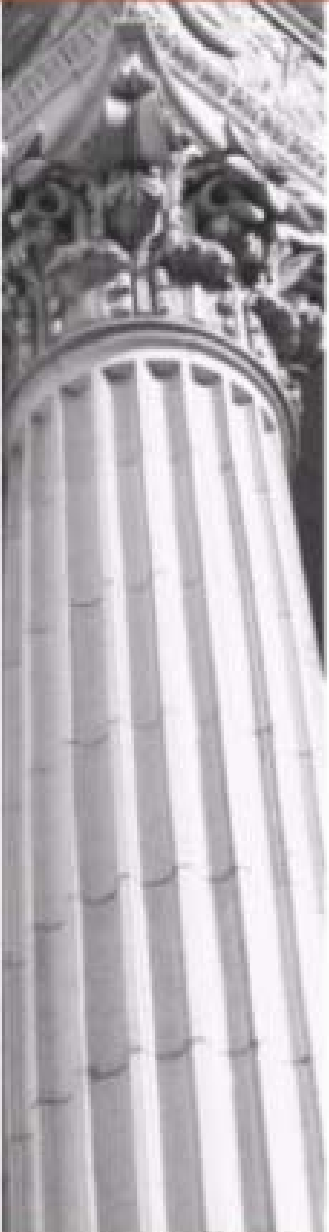






## Governor Snyder's Message to the Legislature

- Emphasis on quality of place in state-local interactions
  - Tie state departments/programs to services provided by local governments
- New hoops for CVTs to jump through to get state revenue sharing
  - Statutory revenue sharing only
  - Only for cities and charter townships still qualifying
  - After adjusting for new census numbers





## Revenue Sharing Hoops

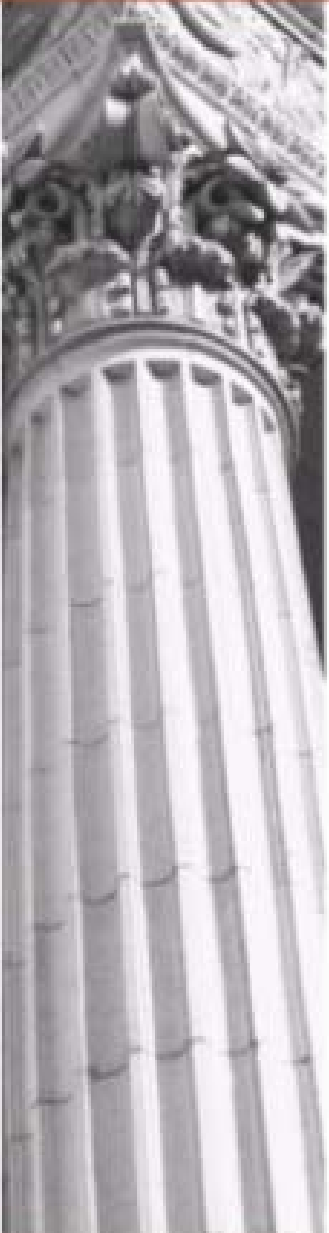
- **Accountability and Transparency**
  - [www.michigan.gov/documents/snyder/LocalGovernmentDashboard\\_348149\\_7.pdf](http://www.michigan.gov/documents/snyder/LocalGovernmentDashboard_348149_7.pdf)
- **Also look to:**
  - GASB – Service Effort and Accomplishment Reporting for Government  
[www.seagov.org/index.shtml](http://www.seagov.org/index.shtml)
  - AGA – Performance and Accountability  
[www.agacgfm.org/performance/performancedefault.aspx](http://www.agacgfm.org/performance/performancedefault.aspx)
  - National Performance Management Advisory Commission  
<http://pmcommission.org/>





## Revenue Sharing Hoops

- Plans to Consolidate Services
  - Existing collaboration counts
  - "Good Faith Effort"
  - Otherwise undefined





## Revenue Sharing Hoops

- Address Employee Compensation
  - All new hires in defined contribution or hybrid retirement plan
  - 1.5% multiplier for defined benefit plans (2% w/o social security benefits)
  - Controls to avoid pension spiking
  - All new hires on an 80/20 employer/employee health care premium split

4/13/11 Gongwer News Service – SJR C and SB 7 to require public employees to contribute at least 20% of health care costs won approval from the Senate Reforms, Restructuring and Reinventing Committee on party-line votes. The measures would impact cities, townships, counties, villages, school districts, intermediate school districts, charter schools, public universities, community colleges, the state and any other public employee.





## Governor Snyder's Message to the Legislature

- Other parts of message
  - Enable consolidation of jurisdictions
  - Ensure collective bargaining at right time
  - Amend PERA
  - Reform PA 312 Binding Arbitration
  - Prohibit minimum staffing requirements
  - Local pension best practices
  - Unfunded Mandate reform





## Take Aways

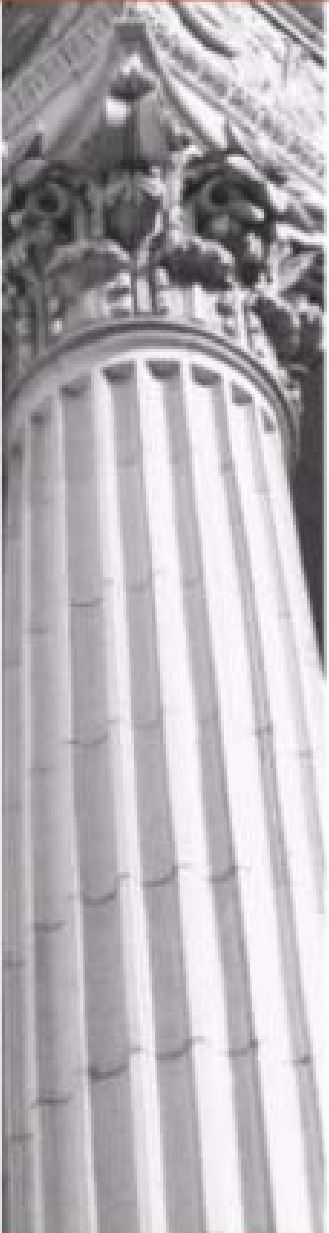
- Local Governments have severe revenue problems
  - Property Tax system in great need of reform
  - If state revenue sharing will not be funded, it should be replaced with regional taxes to be shared among local governments





## Take Aways (pt. 2)

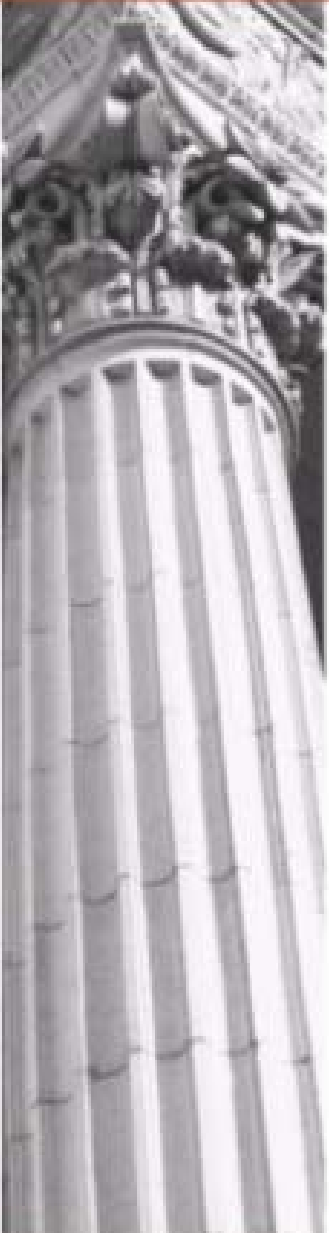
- Reforms proposed by Governor Snyder will be helpful, but will not help enough
  - Accountability is needed, but at this point we are reporting how fast ship is sinking
  - Consolidation of governments and service providers can achieve economies of scale, but result is only marginal savings
  - Reform of labor costs most helpful, but don't expect public employees to "do more with less" at same time they are being denigrated



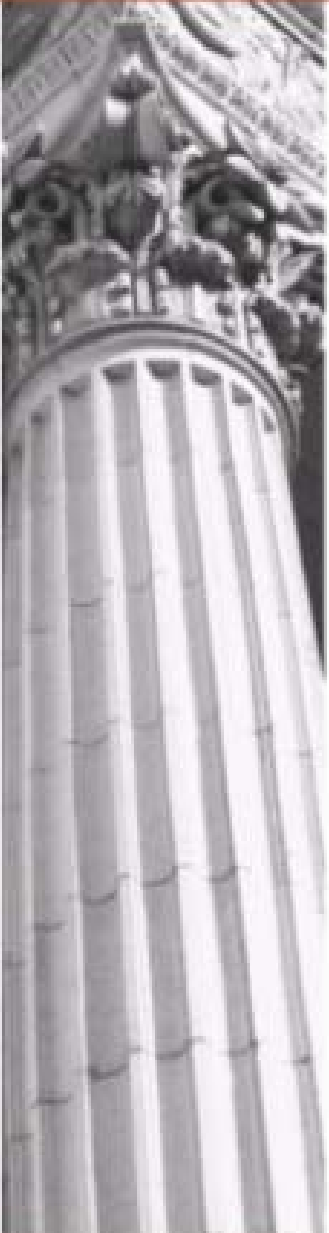


## Take Aways (pt. 3)

- Need Blue Ribbon task force to address level of government responsible for delivering specific services
- Need to reform governance of counties to empower and build confidence
- Need to reexamine regions to align with geography, travel patterns, etc.
- **Don't let a good crisis go to waste!**







**Thank You for your attention**

**Questions?**

**[www.crcmich.org](http://www.crcmich.org)**

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