



A DISTINCTION WITHOUT A DIFFERENCE: AD VALOREM SPECIAL ASSESSMENTS AND PROPERTY TAXES

This paper accompanies a longer paper, *A Distinction without a Difference: Ad Valorem Special Assessments and Property Taxes*. That paper is available at crcmich.org/a-distinction-without-a-difference-ad-valorem-special-assessments-and-property-taxes/.

Key Takeaways

- Property taxes are used to fund general services, while special assessments exist to finance infrastructure improvements that benefit a limited number of properties. In recent years, local governments have increasingly turned to ad valorem special assessments to finance general services.
- Ad valorem special assessments are apportioned on property value and levied similar to the general property tax, but they are treated like an assessment and skirt many of the tax limitations contained in law. While their use to finance local government services is technically legal, it undermines the legal and practical distinctions between taxes and special assessments.
- Beside the policy question of whether ad valorem special assessments should be returned to their historic role, their availability to select local governments is unfair to other local governments that are supporting the same general services through property taxes and to taxpayers as their use circumvents tax limitations under state law and distorts the purpose of the special assessment.
- Ad valorem special assessments should not be maintained in their current form. State policymakers should eliminate statutory authorization for all unit-wide ad valorem special assessments and address the broken municipal finance system so that ad valorem special assessments will no longer be needed. If tax capacity is an issue, local governments should establish emergency service authorities under the process allowed for in state law since the majority of these special assessments fund public safety services.

Summary

Michigan local governments rely heavily on the taxation of property to fund services, infrastructure, and capital improvements.^a **Figure 1** shows that taxes and assessments on land and property in Michigan generally fall into one of four categories that can overlap and range from general ad valorem^b property taxes (far left) to traditional special assessments (far right). Both general property taxes and traditional special assessments have a proper role in the financing of government services and projects. Property taxes are used by all types of local governments to fund various services. Traditional special assessments are levied on parcels of property within limited, specific geographic areas that benefit from capital improvements.

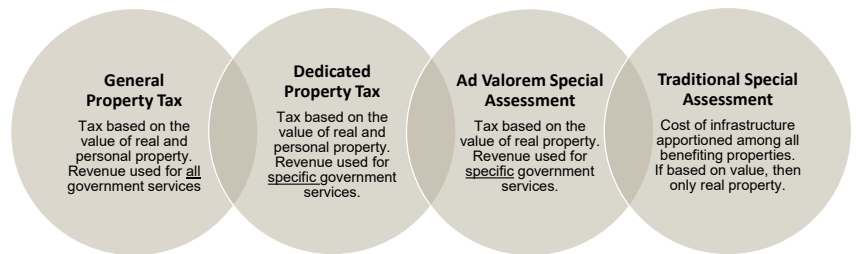
Recently, local governments have increasingly turned to ad valorem special assessments to finance services (mostly police and fire services), a type of special assessment based on the value of property similar to the property tax. While clear legal distinctions exist between general property taxes and special assessments, ad valorem special assessments blur the lines and allow certain local units to use them to finance general government services with an “assessment” that is not subject to the same restrictions as general property taxes. This is unfair to other local governments that are supporting the same general services through property taxes. Further, this is unfair to taxpayers as their use circumvents tax limitations under state statutory and constitutional law and distorts the original purpose of special assessments.

identified generating at least \$18.2 million in revenue; in 1995, the total was 147 districts with at least \$55.5 million in revenue; by 2018, the total reached 246 district levies by 192 local governments (11 percent of the 1,773 cities, villages, and townships in Michigan) with \$195.2 million in revenue.

For the most part, previous recommendations made by the Citizens Research Council to address the use of ad valorem special assessments as a substitute for general property taxes have been ignored by local governments and state policymakers. Local governments, some of whom are facing real fiscal challenges, are using them instead of general property taxes because the law has extended their use for basic governmental services. This legislative action has had the effect of eroding the critical connection between special assessments and public improvements which, in turn, undermines the distinction between special assessments and general taxes.

This hybrid form of property taxation is convenient to address local funding needs, but largely ignores much deeper problems in the design and functioning of Michigan’s local finance system. State law and policy has greatly limited the revenue options available to locals and for many, these special assessments are the only tool they can employ. However, ad valorem special assessments should not be the solution to Michigan’s municipal finance problems.

Figure 1
Four Types of Property Taxation



This is not a new problem. In 1983, 87 ad valorem special assessment districts were

- a The types of property taxes discussed here do not include debt millages, which are unlimited and do not count against millage limitations.
- b Ad valorem comes from Latin and means “to the value.”

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Legal Distinctions between Property Taxes and Special Assessments

While allowing special assessments to be levied for general government services is politically expedient, property taxes and special assessments are not the same and should not be treated as such. A number of court cases shed light on the legal distinctions between property taxes and special assessments and provide clear definitions of each.

Special assessments are based on the theory that capital improvements provide special benefits to some property above that which the general public enjoys.¹ True special assessments can only be levied on land and premises (not personal property); cannot be made a personal liability of the person assessed; are based wholly on benefits; and must be exceptional as to both time and locality.² The properties subject to a special assessment must receive some special benefit from the improvement differing from the benefit the general public enjoys.³

Taxes, on the other hand, are defined as a charge on all property, real and personal, within the taxing jurisdiction.⁴ Taxes are levied to raise revenue for the general operation of government and to benefit the general public; they are compulsory in nature.⁵

Despite these clear distinctions, ad valorem special assessments have been upheld in courts for specious reasons. One court reasoned that they pass muster because they are not levied on personal property.⁶ Another approved their use because it believed that an ad valorem basis for determining the benefit of a fire department was fair.⁷ These rulings ignored key aspects of previous case law providing the distinctions between general property taxes and special assessments. They seem to defer to the legislative intent in passing state laws allowing for ad valorem special assessments rather than to analyze whether the levies in question met the requirements in case law to be considered assessments rather than taxes.

Constitutional and Statutory Distinctions

In addition to the distinctions outlined in case law, general property taxes are subject to numerous constitutional and statutory restrictions that special assessments are not subject to. This includes con-

stitutional requirements for uniformity in assessment and equalization, rate and base limitations, and the statutory processes for appealing taxes and assessments. Special assessments are not subject to the constitutional and statutory property tax limitations on growth, such as the Headlee Amendment and Proposal A.

Special assessments are levied on all real property, including property normally exempt from the general property tax (churches, hospitals, not-for-profits, etc.), unless that property is exempted in the authorizing statute for the special assessment. Special assessments are levied only on real property and are not levied on personal property. The exemption of personal property from special assessment levies serves to shift part of the financial burden of taxes and assessments on property from businesses to homeowners and other real estate owners because residential personal property has long been exempt from taxation. This was a critical distinction prior to the personal property tax reforms in 2012⁸; these reforms have tempered this shift, but many businesses are still paying taxes on personal property.⁹

In their purest forms, property taxes support general government services while special assessments are essentially a financing tool used to support physical improvements to infrastructure. General property taxes are levied unit-wide while traditional special assessments are levied only within a special assessment district comprised of the land and premises especially benefited. General property taxes are levied on a modified acquisition value (taxable value) until there is a transfer in ownership; at which point, they are levied on state equalized value (SEV—50 percent of true cash value). Traditional assessments are generally apportioned on the basis of front footage or land value or area. Most property taxes require voter approval while traditional special assessments do not require voter approval; however, they do require public notice. Finally, general property taxes have a more transparent and easy to understand appeals process while the creation of special assessment districts are presumed valid and can only be appealed at certain times during the process.

Practically, the legal distinctions between property taxes and special assessments are often blurred by ad valorem special assessments, which are levied

more similarly to taxes even though they are not subject to the same restrictions as general taxes (see **Table 1**).

Table 1
Differences between Property Taxes and Special Assessments

	General Property Taxes	Ad Valorem Special Assessments	Traditional Special Assessments
Size of District	Unit-wide	Unit-wide	Land and premises specially benefited
Basis of Levy	Taxable value (modified acquisition value)	Taxable value; sometimes SEV (50% of cash value)	Market value increase in property; costs generally apportioned by front footage or land area/value
Voter Approval Required?	Yes, unless authorized by existing law	Optional with governing board or demanded by petition	No, unless demanded by petition
Property Included in Levy	Real and tangible personal property	Land and premises; sometimes exempts property exempted from general property tax	Land and premises; does not exempt property exempted from general property tax
Rate Limited?	Yes	No	No
Subject to Headlee Rollbacks?	Yes	No	Headlee rollback provisions are not applicable
Proceeds Used For	Basic municipal services or infrastructure improvements	Basic municipal services or infrastructure improvements	Finance physical improvements to infrastructure
Appeals	Appeals process transparent and easy to follow	Appeals process difficult; presumed valid	Appeals process difficult; presumed valid

Ad Valorem Special Assessments in Michigan

Issues surrounding the use and treatment of ad valorem special assessments have been a policy concern dating back to the 1980s with little resolution. In the meantime, their use has only grown. State laws enacted in recent years have served to clarify how they are levied (e.g., specifying that they be levied on taxable value), but not to restrict their use. In fact, some have advocated for expanding the use of ad valorem special assessments to local governments that are not currently allowed to levy them. Despite the seeming popularity among local units that employ this financing strategy, ad valorem special assessments should not be the answer to local governments’ fiscal challenges.

In 2018, there were 246 ad valorem special assessment districts with \$195.2 million in revenue. Ninety percent were created to fund some type of public safety service and 97 percent of the revenue from ad

valorem special assessments goes towards public safety services. Most are levied under Public Act (PA) 33 of 1951 (Act 33), which allows townships and small cities to levy special assessments to fund public safety equipment and services. The majority of ad valorem special assessments are levied by townships (see **Chart 1** on page 5).

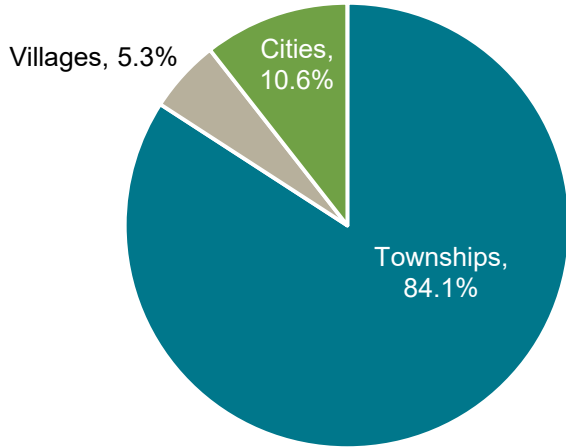
The average ad valorem special assessment rate in 2018 was 2.2257 mills.^c Many townships levy higher special assessment millage rates than general property tax millage rates. While all but two cities^d levying an ad valorem special assessment have higher general property tax rates^e, they are not precluded from having high special assessment levies as well. A number of cities and townships are

c A mill is a term of taxation. It means \$1 of taxation for every \$1,000 of value.

d Ecorse and Saginaw

e General taxes levied excludes levies for debt millages.

Chart 1
Types of Local Units Levying
Ad Valorem Special Assessments



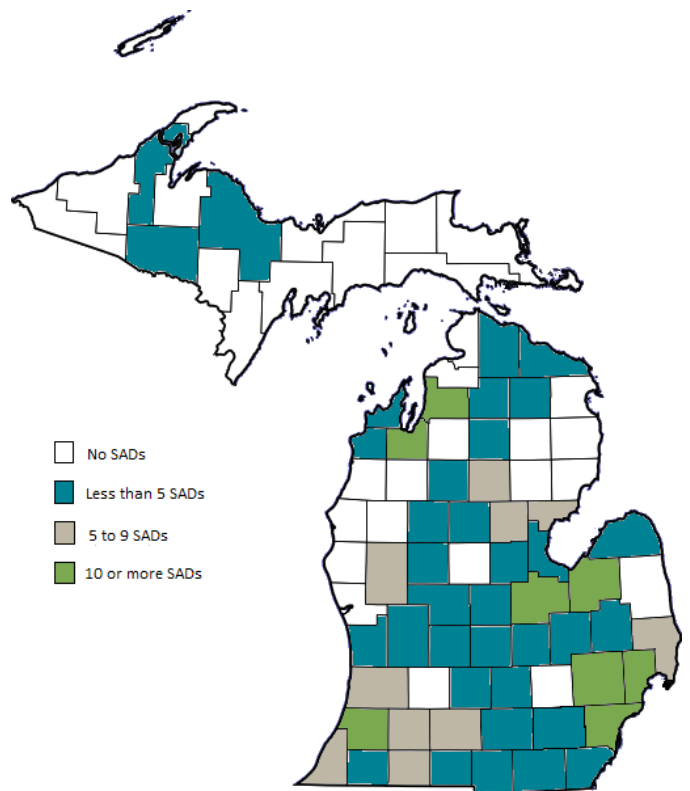
Source: Michigan Department of Treasury

at or near their maximum general property tax rate and may be using special assessment levies to get around tax limitations.

Map 1 shows that almost half of all special assessments (46 percent) levied in 2018 were by local governments (small cities or townships) in eight counties across the state, ranging from rural counties to the populous counties of Southeast Michigan. The remaining 54 percent of local governments levying unit-wide special assessments are located in 45 counties; 30 counties do not have any local units levying an ad valorem special assessment.

Possible reasons for the increased use of ad valorem special assessments over the years include the fact that Act 33 assessments for public safety purposes have become even easier to levy due to further changes in state law. Also, the fact that Act 33 assessments, as well as those levied under other state laws, are not subject to Headlee rollbacks creates an incentive to levy them because they have greater long-term growth potential due to the fact that their rates will not be rolled back. Additionally, economic struggles throughout the 2000s have created fiscal challenges for local governments. Decreases in state revenue sharing coupled with declining property tax revenues for many locals have contributed to a municipal finance crisis and helps explain why more local units might turn to ad valorem special assessments to fund services.

Map 1
 Number of Ad Valorem Special
 Assessment Districts per County in 2018



Source: Michigan Department of Treasury

Recommendations

While the use of ad valorem special assessments to finance local government services is technically legal, it undermines the legal and practical distinctions between taxes and special assessments. It also can be considered inherently unfair to allow a limited number of local governments to fund general government services through ad valorem special assessments rather than general taxes, which are subject to constitutional and statutory restrictions on their levy. With ad valorem special assessments, the linkage between property value and benefits is tenuous at best and the differences between the two types of levies can lead to taxpayer confusion. Despite this, state policymakers have continued to open the door to allow for the use of ad valorem special assessments.

The Research Council offers three recommendations to address the use of unit-wide ad valorem special assessments:

- 1) State policymakers should eliminate statutory authorizations for unit-wide ad valorem special assessments. Special assessments should be levied only for recuperating costs that increase the market value for specific properties; they should not be unit-wide and

they should not support general government services.

- 2) Local governments using ad valorem special assessments may establish emergency service authorities to provide police and fire services.¹⁰ Establishment would require local authorization to levy a property tax to support public safety services. The tax rate would be subject to the millage limitation established by the voters. This would require the local government to join with another local government to create a multi-jurisdictional authority.
- 3) State policymakers should rethink municipal finance and governance, including authorizing new local-option taxes in state law and requiring a more regional focus on new taxes and local government service delivery. If the property tax is not sufficient to meet local own-source revenue needs, then local governments need more revenue options, which could include sales or excise, income, transportation, "sin", or other specific taxes. Additionally, the state and local governments should take a serious look at the municipal finance and service delivery system, which has not changed much since the 1800s despite advances in transportation, communication, and technology

Conclusion

The problem addressed in this paper is not with all special assessments, but with the hybrid ad valorem special assessment, which is levied like a tax, but regulated like a special assessment. Traditional special assessments provide a financing option for needed capital improvements within a local unit of government. General government services that are provided unit-wide should be funded from tax

revenues. Ad valorem special assessments have become a Band-Aid for local governments that allows state and local officials to avoid the hard issue of the broken municipal finance system. Addressing this issue will require state and local officials to rethink how local government is structured, how it is funded, and how services are provided.

Endnotes

- 1 City of Lansing v Jenison, 201 Mich 491, 497; 1918.
- 2 Blake v Metropolitan Chain Stores, 247 Mich 73, 77; 225 NW 587; 1929.
- 3 City of Lansing v Jenison, 201 Mich 491, 497; 1918.
- 4 Blake v Metropolitan Chain Stores, 247 Mich 73, 77; 225 NW 587; 1929.
- 5 Bolt v City of Lansing, 459 Mich. 152; 1998.
- 6 St. Joseph Township v Municipal Finance Commission, 351 Mich 524 (1958).
- 7 Niles Township v Berrien County Board of Commissioners, No. 244138, March 23, 2004 (<https://caselaw.findlaw.com/mi-court-of-appeals/1457579.html>, accessed 1/17/19).

- 8 PublicActs (PA) 397-408 of 2012 and PAs 489-490 of 2013.
- 9 Citizens Research Council of Michigan. Memorandum #1126: "Statewide Ballot Issues: Proposal 2014-1 Voter Approval of a New Statewide Local Tax to Reimburse Local Governments for PPT Reform," July 2014 (https://crc-mich.org/personal_property_tax_reform_question-2014/).
- 10 Emergency Services to Municipalities, PA 57 of 1988 (MCL 124.601 et seq.), www.legislature.mi.gov/mileg.aspx?page=getObject&objectName=m-cl-Act-57-of-1988

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