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### ARE JUDGMENT LEVIES, JUDGMENT BONDS, AND OTHER TAKES AUTHORIZED WITHOUT LIMITS PERMITTED UNDER THE MICHIGAN CONSTITUTION?

The Michigan Constitution limits directly or requires the Legislature to limit the power of local governments to tax and incur debt, and it calls for voter approval of local taxation and borrowing. However, authority to levy taxes outside existing limits has been granted by the Legislature over the years, and today unlimited property taxes may be levied without voter authorization by the local legislative body or pursuant to a court order in virtually all local units of government in Michigan.

For example, in June 1984 the Wayne County Circuit Court, under the authority granted by the Revised Judicature Act (PA

236 of 1961), ordered the City of Hamtramck to impose a one-year judgment levy of 9.6 mills to pay approximately \$1.4 million in "back-pay" due to the city's police and fire personnel from an arbitration award. The tax imposed was in excess of the property tax rate authorized by the local electorate in the city charter. In fact, the citizens of Hamtramck voted down a property tax increase to finance the arbitration award the day before the court ordered the judgment levy. The Circuit Court recently ordered two additional judgments for employee compensation and benefits totaling 15 mills to be levied on 1987 tax bills, in addition to the city's regular operating tax rate.

This **Council Comments** focuses on the, primary issue raised by all such laws: Does the Michigan Constitution give the Legislature power to authorize, local governments to impose taxes and contract debts without voter approval and without or outside defined limits? A strong argument can be made that such, laws violate the spirit, if not the letter, of constitutional provisions on local government in Article 7 and the powers

to tax in Article 9 of the 1963 Constitution (and similar provisions in the 1908 Constitution). As this report will demonstrate, with some minor modifications these laws can be reconciled with the spirit of this state's framework for local tax limits, preventing profligate local governments from incurring obligations without limit and having the court present the past-due bill to the local citizens.

This **Council Comments** summarizes a more comprehensive report on this subject

(Report No. 284, 52 pages), copies of which are available on request.

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## A HISTORICAL OVERVIEW OF TAX LIMITS AND LOCAL HOME RULE IN MICHIGAN

**Fiscal Limits and the Beginnings of Local Government in Michigan.** As early as 1850, the citizens of Michigan authorized the Legislature to provide by law for the creation of cities and villages. The citizens of Michigan also placed certain requirements on the Legislature when exercising this authority. Article XV, Section 13, of the 1850 Constitution stated: “The Legislature shall provide for the incorporation and organization of cities and villages, and shall restrict their powers of taxation, borrowing money, contracting debts, and loaning their credit.” Under the 1850 Constitution, the Legislature would grant a “municipal charter” by enacting a “local act.” A separate act was adopted for each municipality, and the “charter” could only be altered or amended by the state Legislature.

As required by the Constitution, each municipal charter contained limits on the municipality’s ability to impose taxes and contract debts. Since Michigan’s constitutional declaration of rights prohibited the Legislature from enacting a law impairing the obligation of a contract, municipalities were authorized to incur debt and impose general taxes up to certain limits, and to impose debt taxes without limit to repay legally incurred debt. Although municipal charters technically authorized an “unlimited” tax for debt retirement, the tax was, in fact, limited since the ability to contract debt was limited.

The Michigan Supreme Court held these provisions to be crystal clear in intent, holding in several decisions that:

1. The Legislature had an imperative duty to impose tax and debt limits on cities and villages.
2. Taxes for general operating purposes

could not exceed the statutory limits, although local units could levy taxes up to those limits.

3. Cities and villages could not incur debt exceeding the constitutionally required, legislatively established limits, and once debt was issued, sufficient taxes must be imposed to repay the debt.
4. A contract with a municipal corporation was valid only if the municipal corporation had the legal authority to raise by taxation the amount which it had agreed to pay -- the right to contract was limited by the right to tax.

**Home Rule and the 1908 Constitution.** Home rule was first authorized in Michigan by provisions in the 1908 Constitution which required the Legislature to provide for the incorporation of cities by adopting “a general law” that authorized local citizens to frame, adopt, and amend a city charter. The general law adopted by the Legislature must also limit the rate of taxation imposed by a city for municipal purposes and restrict its power to borrow money and contract debt. It is crucial to understand the relationship of these requirements: there must be a tax limitation and a debt limitation, both of which must be placed in the general act providing for the incorporation of a city through the process of drafting and adopting a charter by the local electorate. The Constitution required the Legislature to adopt a similar law for villages.

Pursuant to the constitutional mandate of local home rule, the Legislature adopted the Home Rule Cities Act providing that a municipal charter adopted by the local electorate could authorize taxes of up to 20 mills for operations and could authorize the issuance of debt of up to eight percent of assessed value, with unlimited taxing authority to repay the debt and voter approval required for each specific debt issue. Two ex-

ceptions to the debt limit were authorized -- mortgage bonds to own and operate a public utility, if the debt did not impose a liability on the city, and emergency bonds in limited amount and duration. While these bonds were not subject to the general limits, they were, however, subject to specific limits.

Again the courts had little trouble interpreting the intent of these provisions, holding that:

1. Since the Constitution required the Legislature to limit the power of cities and villages to tax and contract debt, it also by implication authorized the Legislature to raise or lower the limits as it saw fit, subject to charter amendment by the local electorate if the limits were increased. The Legislature could alter these powers at any time, so long as the change did not impair the repayment of existing obligations.
2. The Constitution did not require the Legislature to place debt limits on negotiable obligations such as mortgage or revenue bonds because no debt, and no obligation, was incurred directly by the issuing jurisdiction.

The 1908 Constitution, like the 1850 Constitution, was silent on the subject of the taxing and borrowing powers of counties, townships, and school districts. It is also important to note that at this time most activities of state government were financed from a statewide property tax which had no limitations specified in the Constitution.

**The First Property Tax Revolt.** In 1932, during the depths of the Great Depression, an initiative petition was adopted by the electorate which amended Article 10 (the fi-

nance and taxation article) of the 1908 Constitution by adding Section 21. For the first time in the history of the state, strict limitations were placed in the Constitution on the amount of property tax that could be levied without voter approval.

The Supreme Court ruled the intent of the amendment was to provide a general limitation on the state from imposing or granting local units of government authority to impose property taxes without voter approval. Specifically, the state and unchartered local units of government could levy, without voter approval, a combined total of up to 15 mills. With voter approval, these units could levy up to 50 mills. These units were also authorized to levy property taxes without limit as to rate or amount, sufficient to pay the annual principal and interest on bonds issued prior to the adoption of the tax limitation amendment. After the adoption of the tax limitation amendment, units of government subject to the 15- and 50-mill limit could not issue general obligation bonds without voter approval to increase the constitutional property tax limits. These units of government must also pay any court ordered judgments, and absent a vote to increase the constitutional limit, the judgment must be paid from within the allocated millage.

Taxes levied by cities and villages were outside the 15- and 50-mill limits, but were subject to voter approved limits established in the locally drafted and adopted charter. That is, the citizens of Michigan were protected by the Constitution from taxes levied in excess of 15 mills (excluding pre-1932 debt) without their consent. The local electorate could exchange this constitutional protection for the tax limitations in a local charter which also, by constitutional direction, afforded protection from taxes levied without voter approval.

### **The Age of “Generated Public Necessity” Leads to the Vacillating Court.**

Although the tax limitation provisions of the Michigan Constitution appeared fairly restrictive and quite simple in the 1930’s, a series of legislative actions and court interpretations in the 1940’s and 1950’s led the Supreme Court to conclude that “the 15-mill amendment has been bruised, beaten and backed to the brink of sterile and forceless words...[by] [b]ench law made of generated public necessity and pressured regression . . . .”

In a series of decisions involving the City of Port Huron, the Supreme Court ruled that taxes could be imposed outside of tax and debt charter limits by a court order when the court deemed the expenditures to be necessary. The Court also sanctioned the Legislature’s release of local units of government other than cities and villages from the 15- and 50-mill limitations by permitting the local unit to adopt a state law as its local “charter.” And the Court held that drain taxes were subject to the constitutional limits in nonchartered units but could be imposed outside of any statutory or charter limits in chartered units.

On the other hand, the Court did reaffirm that court-ordered judgments against non-chartered units are to be levied from within the constitutional tax limits, and in the late 1950’s the Court began a retreat from the assault on property tax limits. It rejected a legislative attempt to create other “charter” authorities, declaring that in the future only local units qualifying under the historic definition of the term ‘municipal corporation’ could be released from the 15- and 50-mill limits. Shortly thereafter, the Court issued a strongly worded opinion on a legislative attempt to circumvent the constitutional limit on the state sales tax which said that the “most pressing rule for constitutional construction” is that “the provisions for the protection of life, liberty and property are to

be largely and liberally construed in favor of the citizen.”

### **The 1963 Constitution -- “The Property Taxpayers of Michigan Were Yensed.”**

The 1963 Constitution made minor changes to the home-rule provisions of the 1908 Constitution. The new wording is as follows: “The legislature shall provide **by general laws** for the incorporation of cities and villages. **Such laws** shall limit their rate of ad valorem property taxation for municipal purposes, and restrict the powers of cities and villages to borrow money and contract debts. Each city is granted power to levy other taxes for public purposes, subject to limitations and prohibitions provided by this Constitution or by law” (Article 7, Section 21; emphasis added). Note that in modernizing the language the drafters created ambiguity as to whether there must be a single law for city incorporation (and another for villages), and whether that law must also contain tax and debt limits; nevertheless, it is clear from the record that the intent was to continue such requirements.

In a definitive statement concerning the authority of the Legislature under Article 7, Section 21 (and similar language pertaining to charter counties in Article 7, Section 2), the Michigan Supreme Court said in a 1972 decision: “As to chartered counties the Legislature is under a constitutional duty to restrict their power to borrow money and contract debt. See Const 1963 art 7, sec 2. The Legislature is under a similar duty with respect to cities and villages under Const 1963 art 7, sec 21. As to chartered counties, cities and villages therefore any statute which provides an unlimited ability to contract “debt” would be in violation of the constitutional provision requiring the Legislature to limit the ability of these entities to contract debt” (emphasis added). Since the Constitution requires the Legislature to limit the authority of these units (cities, villages, and charter counties) to impose ad valorem property

taxes, any statute which authorizes an unlimited property tax would also violate the Michigan Constitution.

The new Constitution created two exclusions from the 15- and 50-mill tax limitation provisions: (1) “taxes imposed for the payment of principal and interest on bonds or other evidences of indebtedness or for the payment of assessments or contract obligations in anticipation of which bonds are issued, which taxes may be imposed without limitation as to rate or amount...”; and (2) “taxes imposed for any other purpose by any city, village, charter county, charter township, charter authority or other authority, the tax limitations of which are provided by charter or by general law.” (Article 9, Section 6)

Although the drafters claimed they had continued in substance the 15-mill limit, the Court unanimously disagreed, holding that the first exclusion permitted all local units to impose unlimited taxes to repay indebtedness; all but one justice concluded that such taxes could be levied without voter approval. The Court also ruled that an operating deficit (considered to be an “other evidence of indebtedness”) could be repaid with taxes imposed outside the 15- and 50-mill limits and without voter approval.

**The Second Property Tax Revolt.** In 1978 the voters approved an amendment to the 1963 Constitution that, among other things, closed the indebtedness exception noted above. The so-called Headlee amendment allowed unlimited taxes without voter approval to continue for bonds issued prior to the adoption of the amendment. Bonds issued subsequent to the amendment, however, required voter approval if unlimited taxes were pledged for debt service.

The amendment also prohibited local governments from levying “any tax not authorized by law or charter when this section is

ratified or from increasing the rate of an existing tax above that rate authorized by law or charter when this section is ratified” without voter approval. Subsequently, the Court of Appeals held that the power of the courts to require tax levies in settling judgments must be harmonized with this tax limitation amendment, but gave little more than a hint as to the direction that must be followed.

### **WHERE LOCAL GOVERNMENT CONSTITUTIONAL TAX AND DEBT LIMITS STAND TODAY**

The current tax and debt limitations on local units of government in Michigan are as follows:

- ❖ For noncharter units of government, operating millage without voter approval is limited to a total of 15 mills. This limit may be increased to a total of not to exceed 50 mills for a period of 20 years with voter approval. Unlimited taxes in excess of the 15- and 50-mill limits may be levied to repay bonds issued, with voter approval, after December 23, 1978, or bonds issued with or without voter approval before that date.
- ❖ For cities, villages, and charter counties, the Constitution requires that the general law that provides for the incorporation of these units also limit their powers of taxation, borrowing money, and contracting debts. Taxes imposed for purposes other than debt retirement are not subject to the 15- and 50-mill constitutional limitations, but rather to the limits provided in the general law and incorporated in the locally adopted charter. Taxes imposed for purposes other than debt retirement by the so-called “charter authorities” are limited by state statute and/or voter approval. As with non-

charter units, the taxes imposed by cities, villages, charter counties, and other charter authorities may be levied to repay bonds issued, with voter approval, after December 23, 1978, or bonds issued with or without voter approval before that date.

There are several state statutes which authorize local government taxes and the contracting of debt that conflict with the spirit if not the letter of these limitations.

- ❖ **Unlimited judgment levies and judgment bonds authorized in the Revised Judicature Act and Court Ordered Bond Act:** The Constitution does not authorize the Legislature to permit the levying of unlimited property taxes, the contracting of unlimited debt, or the contracting of general obligation debt without voter approval in any local units, or the levying of taxes above 15 mills in nonchartered units without voter approval.
- ❖ **The local garbage tax (PA 127 of 1976):** The garbage tax authorization is not a part of the Home Rule Cities Act, and the 3-mill tax is levied without voter approval and outside the 20-mill charter limit.
- ❖ **Unlimited debts authorized in the Home Rule Cities Act, Incorporation of Villages Act, and Charter Townships Act:** The Constitution requires the Legislature to limit all forms of general obligation municipal debt.
- ❖ **Drain taxes authorized to be levied without limits in charter units:** The Constitution requires the Legislature to establish limits, and the constitutional scheme calls for such limits to be placed in the Home Rule Cities Act and similar laws for other charter units.

- ❖ **Unlimited tax and bonding authority in the County Public Improvement Act; Sewage Disposal, Water Supply and Solid Waste Management Act; and Sewage Disposal and Water Supply Districts Act:** The Constitution requires that tax and debt limits be placed on cities, villages, and charter counties by the Legislature and places direct limits on imposing taxes or issuing debts without voter approval by townships and general law counties.

#### RECONCILING TAX LIMITATIONS AND THE PAYMENT OF GOVERNMENT OBLIGATIONS

Although the only short-run solution to the imposition of property taxes without voter approval is challenges mounted by individual taxpayers, in the long-run the concept of tax limitation must be harmonized with the payment of legally incurred government obligations. This is especially true of taxes imposed pursuant to a court order requiring a judgment levy or the sale and repayment of judgment bonds. Unfortunately, the judgment statute has the potential to subvert the constitutionally prescribed fiscal system of local government whereby the local citizens give to the government a fixed amount of money from within which the government is to provide municipal services. This law makes possible a process whereby a profligate local government incurs obligations without limit and has the court present the past-due bill to the local citizens.

The imposition of taxes without the consent of the governed is certainly not a recent issue. In Michigan, as long ago as 1879, the Supreme Court ruled in the case of **Wattles v City of Lapeer** that taxes cannot be levied in excess of the limit expressly fixed by law. While the Revised Judicature Act does not explicitly state that court-ordered judgments are to be imposed outside of voter author-

ized limits, unfortunately this has become an accepted practice in recent years.

Property tax limits expressly fixed by law would be respected if the courts only authorized the tax collecting agent of the government to set aside a portion of the next regular property tax levy sufficient to satisfy the judgment. The judgment would be paid, therefore, from within the taxing authority granted by the voters. This would turn the judgment statute from what some have interpreted to be a law granting the judiciary independent taxing authority to a law granting the judiciary power to “garnishee” a part of the next property tax levy of the local government. It would also put local public officials on notice that they no longer have an unlimited charge account at taxpayer expense, and that they are required to finance government operations from within existing revenue sources.

A recent Benton Harbor case can be used for illustrative purposes. In August 1984, the Berrien County Circuit Court ordered the city to impose a judgment levy each year for the next thirty years to finance a \$2.6-million unfunded liability in the police and fire pension fund. This amounted to a 4.25-mill property tax in 1985. With a city charter authorized tax limit of 20 mills for municipal purposes, the court order could have required that 4.25 mills of the 20-mill property tax be contributed to the pension fund. The city would then have been required to finance municipal services with the remaining 15.75 mills, rather than being able to levy 20 mills for municipal services and an additional 4.25 mills for the pension fund. The satisfaction of the judgment, in effect, would become a first budget obligation in the fiscal year following the judgment order. Under this arrangement, the legally incurred obligations of the government would have been satisfied without exceeding the voter-approved tax limits. This kind of harmonizing of the two requirements was set forth

by the Michigan Supreme Court in the **Morley Brothers** decision in 1945 and continues to be referenced whenever the courts confront such an issue.

The Revised Judicature Act also authorizes the issuance of court-ordered bonds to satisfy judgments, and a similar concept can be used to harmonize the repayment of the bonds with voter-imposed tax limits. If a judgment is so large that a one-time garnishment would inflict financial hardship on the local government, the court could order the issuance of judgment bonds. Repayment of the principal and interest due each year on the bonds would become a first budget obligation -- to be paid from within existing taxing authority. The local government could seek voter approval of the bond issue, thereby pledging the full faith and credit (and unlimited taxing authority) of the issuing governmental unit. This procedure was used by the Dearborn School District in 1985 to satisfy a judgment against the school district involving the overpayment of school property taxes by the Ford Motor Company. Since any judgment bonds impose a direct obligation on the issuing governmental unit, these bonds should be subject to any voter-imposed debt limitation. If the unused debt authority within the limit is insufficient to satisfy the judgment, new bonds could be issued in concert with the retirement of previously issued debt.

This same procedure could be used for bonds issued to construct and maintain sewage systems, solid waste facilities, etc., under the Court Ordered Bond Act. The act currently authorizes local units to issue only revenue bonds (that do not impose any general obligation on the issuing municipality) when the local unit acts without a court order. There seems to be little justification for a court to order the issuance of full faith and credit bonds when revenue bonds (to be repaid from user charges) will serve the same purpose. In addition, the constitutional guar-

antee against the imposition of taxes without the consent of the voters would be protected if the Drain Code, the other acts highlighted in this report, and any other statutes that

grant taxing authority required that these taxes be levied within constitutional, statutory, and charter limitations.