



**MICHIGAN'S UNRESTRICTED REVENUE SHARING PROGRAM:
RETROSPECT AND PROSPECT**

September 2000

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Citizens Research Council of Michigan

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**MICHIGAN’S UNRESTRICTED REVENUE SHARING PROGRAM:
RETROSPECT AND PROSPECT**

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MICHIGAN'S UNRESTRICTED REVENUE SHARING PROGRAM: RETROSPECT AND PROSPECT

Highlights

After nearly two years of deliberation and debate, in December 1998, the Michigan Legislature approved a new set of revenue sharing formulas to distribute more than \$800 million annually to cities, villages, townships, and counties. The new revenue sharing formulas create, as do most significant public policy changes, winners and losers.

Against the general backdrop of potential financial plenty, the following factors represent the highlights of the Citizens Research Council findings:

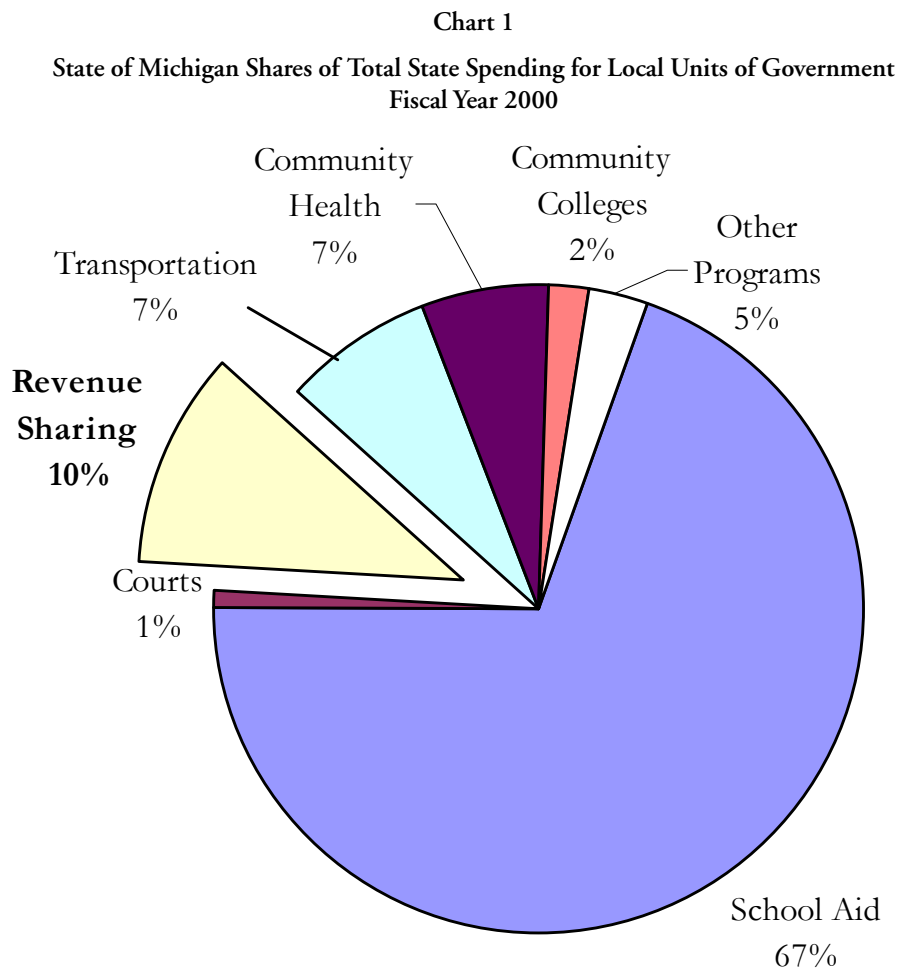
- Generally, individually and collectively, townships and villages gained in share of statutorily defined payments and cities lost share.
- The formulas are extremely complicated, and because of interactions between components of the formulas and individual unit values, projections of individual unit payments must rely on models including all of the nearly 1,800 cities, villages, and townships.
- The somewhat complicated mechanisms intended to smooth the changes over many years and protect units from abrupt decreases in payments generally work. However, another provision removing controls on maximum increases for units with population gains exceeding ten percent will result in a lower floor on payment changes for units who stand to lose payment shares than would have been the case if all units were subject to the same payment controls. This will lessen the cushion against reductions in payments for units facing losses from formula changes and/or population change.
- A recession will more adversely affect units receiving payments under the payment increase cap mechanism than other units. During an economic recovery, units receiving payments under the cap mechanism would benefit vis a vis a non-recession scenario.
- In order to formulate a revised program, special treatment for the City of Detroit was necessary. The bargain Detroit struck has two parts. Its annual payments are frozen at \$333.9 million until June 30, 2007. In exchange for the protection against declining payments afforded by this provision, the personal income tax rates on resident and non-resident taxpayers are reduced by one-third over a ten-year period. This is accomplished in even percentage point decrements each year. While this provision is beneficial to personal income taxpayers, Detroit will have to manage with less general revenue than it would have had if Senate-proposed formulas had been approved. Separating Detroit from the other cities, villages, and townships and freezing its revenue sharing payments for the eight-year duration of the formulas adds a new wrinkle. The growth in revenues that would have been allocated to Detroit had the state's largest city been included in the formula, is available for distribution to the other cities, villages, and townships, creating what social scientists sometimes refer to as a "positive sum" result. In other words, municipal units *in the aggregate*, will benefit compared with the old formula.
- The new revenue sharing formulas are scheduled to expire June 30, 2006, 15 months before the phase-in of the new formulas is completed. If the legislature chooses to continue the plan beyond that date, the payment cap mechanism would need to be continued or another form of safety net implemented in order to avoid significant drops in payment levels for a few units.

Michigan's Unrestricted Revenue Sharing Program: Retrospect and Prospect

I. Introduction

In December 1998, the Michigan Legislature approved a major revision in the State's revenue sharing program. The unrestricted revenue sharing program in Fiscal Year (FY) 2000 will pay over \$1.4 billion to general-purpose local units of government: cities, villages, townships, and counties. These units may use the revenues for any legitimate governmental purpose.

Although counties receive revenue sharing, most revenue sharing dollars are paid to cities, villages, and townships and it is these payments that have attracted the greatest legislative attention and interest and are the focus of this report. The report traces the development of Michigan's program over a six decade period, describes the formula components in place prior to the 1998 revisions, and provides illustrative projections of payments under the new formulas beyond the year 2000.



Source: CRC Calculations from Senate Fiscal Agency data.

II. Michigan's Revenue Sharing Program

A. State Support for Local Government

The State of Michigan provides a broad range of financial support to its local units of government—cities, villages, townships, counties, school districts, and community colleges. Three-fifths of all state-levied taxes, fees and other charges, almost \$15 billion in FY2000, are paid to local units of government. **Chart 1** summarizes the major categories of state aid to local units in FY 2000.

The second largest category of aid after School Aid, unrestricted revenue sharing comprises shared state tax revenues

that are distributed to cities, villages, townships, and counties based on formula calculations. The expenditure of these funds may support any programs the individual unit operates. Over 1,800 local units of government benefit from these revenue allocations, which, for many units, is their largest source of revenue. In FY 2000, over \$1.4 billion is appropriated for distribution to cities, villages, townships, and counties derived from 36.3 percent of the portion of the Sales Tax at a four percent rate.

B. Brief History

Michigan's unrestricted revenue sharing program began in the early 1930s when 85 percent of retail liquor-license tax collections were paid to cities, villages, and townships. In 1939, the state began sharing intangibles tax receipts on a per capita basis with cities, villages, and townships to offset the removal of intangible property from local tax rolls.

1. Constitutional Commitment of Revenues

In 1946, the first significant commitment of shared revenues was made as a result of voter approval of a constitu-

tional amendment earmarking one-half cent of the Sales Tax for distribution to cities, villages, and townships on a per capita basis. This change has been brought forward, surviving four constitutional amendments affecting the state sales tax and a new constitution, and the approximate equivalent of that half-cent of the sales tax is still distributed to cities, villages, and townships on a per capita basis.

2. Sharing the Income Tax

In 1967, the state implemented new Personal and Corpo-

Figure 1

Milestones in Michigan's Unrestricted Revenue Sharing Program

Year	Event
1933	Unrestricted revenue sharing begins with liquor-license tax collections.
1939	Intangibles Tax is shared to offset loss of intangible property from local tax base.
1946	Constitutional amendment passes. State begins sharing one-half cent of Sales Tax with cities, villages, and townships.
1967	11.5 percent of new State Income Tax shared. One-half goes to counties and one-half to cities, villages and townships.
1972	Distribution of city, village, and township Income Tax payments based on relative tax effort (RTE).
1975	Single Business Tax enacted and shared on RTE basis with cities, villages, and townships. Reimbursement of local revenue loss resulting from removal of business inventories from tax base begins.
1991	State discontinues Intangibles Tax distribution.
1996	State consolidates Income Tax and Single Business Tax shared revenues into an expanded percentage of the Sales Tax. Past revenue reductions in statutory allocations made permanent through lower Sales Tax percentage.
1997	At the beginning of FY1998, growth in the statutory payment allocation is made on a per capita basis. A legislative task force is charged with recommending changes in the statutory formula.
1998	Statutory formulas are repealed and replaced by new formulas with a ten-year phase in period.

rate Income Taxes. Payments from the Personal Income Tax were earmarked for counties, cities, villages and townships. Counties divided 11.5 percent of the gross receipts of the tax equally with cities, villages, and townships on a per capita basis.

Beginning in 1972, the payments from state Income Tax revenues to cities, villages, and townships shifted to a per capita calculation that weighted population by an index of relative tax effort (RTE).

3. The Single Business Tax

Beginning in FY1977, with the removal of inventories from the personal property tax base and the enactment of the Single Business Tax (SBT), payments were made from SBT revenues to offset the revenue loss resulting from the inventory exemption. The inventory reimbursement payments were based on current tax rates times the assessed value of inventories in 1975. By the 1990s, the location and amount of inventory tax base that would have been taxed without the change probably bore little relationship to the 1975 tax base that was still being used to calculate the payments. At the same time, the State began reducing the county share of the income tax and increasing the share going to cities, villages, and townships. The county share dropped to 35 percent by FY1980 with the share going to the other units increasing to 65 percent.

4. A Period of Stability and the Seeds of Change

During the 1980s and through the middle of the 1990s, the revenue sharing distribution methods stayed relatively constant. The amount distributed under the statutory formulas was reduced from time to time, usually in association with budget difficulties experienced by the state.

Although the program was stable, criticism of the statutory distribution formulas, RTE and inventory reimbursement became widespread. It was argued that the RTE formula rewarded high tax rates with increased payments thereby encouraging increases in local taxes.

Much of the criticism was articulated in the form of dissatisfaction with the geographic distribution of statutory payments and the unevenness among cities, villages, and townships. Since tax rates drive the RTE calculation (in FY 1998, each mill of tax effort was worth about \$2.50 per capita) and taxes are generally higher in cities and villages than in townships and in southeastern Michigan than in the rest of

the state, the issue was often debated in those terms. Critics often argued that southeast Michigan communities received too much aid and outstate communities too little. Others argued that townships deserved a greater share of statutory revenues than they were receiving.

In an effort to bring closure to the criticism and debate, the Legislature, in June 1996, passed a bill establishing a bipartisan legislative task force charged with identifying alternatives to the RTE and inventory reimbursement formulas and recommending changes in existing law. In order to encourage resolution, growth in statutory shared revenues were distributed on a per capita basis in FY 1998 and no growth in revenues was to be distributed after FY 1998. Revisions were also enacted that allocated revenues from the four taxes—Income, Sales, Intangibles, and SBT—then part of the overall program. Allocations of Intangibles, Income, and SBT revenues were eliminated and replaced by a new allocation of the sales tax—21.3 percent of the collections at a four-percent rate (about 14 percent of all Sales Tax revenues). That distribution rate captured reductions in the amounts that would have been distributed in FY1997 had the statutorily earmarked revenue sources been fully paid to local units.

The legislative task force was to submit a written report to the legislature by the end of September 1997. Failure by the task force members to reach agreement on recommended changes caused the report to be delayed, and after one formal legislative extension of the deadline, certain task force members introduced legislation reflecting their individual points of view.

5. New Formulas Approved

Finally, in December 1998, legislative leaders and the Governor forged a compromise that became the current law. It reflects a general decision to shift shared revenue payments *gradually* from urban areas to suburban and rural areas, from southeast Michigan to outstate Michigan, and from cities to villages and townships. The changes included in the new legislation will take ten years to be fully implemented. In the interim, a new census will create new population counts and the bill will sunset. For most units, the reflection of the new census counts in FY2001 will cause the largest year-to-year change experienced during the phase-in period. The law containing the new formulas is scheduled to sunset on June 30, 2007.

C. Features of the Old Formulas

Under the old law, statutory payments for cities, villages, and townships were calculated using two formulas. Each formula had its detractors and was subjected to ongoing analysis and criticism.

1. Inventory Reimbursement

A unit's inventory personal property tax base in 1975 was multiplied by the tax rate in the current period and the amount was paid to the unit. This mechanism was intended to compensate units for lost tax revenues associated with the repeal of the inventory tax when the SBT was imple-

mented. The source of State revenue used for this payment was, fittingly, SBT revenues.

The inventory reimbursement mechanism had some very obvious flaws. Since the tax base remained at the 1975 level, the mechanism's ability to compensate local units for their losses in real terms declined over time. In nominal terms, inventory payments increased only 16 percent during a period when the overall property tax base increased 257 percent. Since inventory is no longer measured or reported for property assessment purposes, it is not possible to measure the degree of distortion that has occurred in the

Table 1
Units with Inventory Reimbursements Exceeding \$30 Per Capita in FY1998

Local Unit	County	Inventory Reimbursement Per Capita	Total Revenue Sharing	Percent of Total Revenue Sharing
Townships				
Brownstown	Wayne	\$32.06	\$130.83	24.5
Pte Aux Barques	Huron	45.30	129.31	35.0
Southfield	Oakland	30.63	94.91	32.3
Cities				
Benton Harbor	Berrien	32.19	167.66	19.2
Buchanan	Berrien	44.22	153.90	28.7
Center Line	Macomb	41.01	152.14	27.0
Ecorse	Wayne	62.11	212.97	29.2
Hamtramck	Wayne	40.99	197.51	20.8
Highland Park	Wayne	46.28	225.62	20.5
Imlay City	Lapeer	36.66	144.44	25.4
Marysville	St. Clair	45.35	150.75	30.1
Melvindale	Wayne	33.68	180.66	18.6
Milan	Monroe	54.93	158.83	34.6
Mt. Morris	Genesee	46.05	154.77	29.8
Pontiac	Oakland	55.99	230.58	24.3
River Rouge	Wayne	69.40	195.53	35.5
South Lyon	Oakland	89.34	194.68	45.9
Springfield	Calhoun	36.88	164.86	22.4
St. Joseph	Berrien	43.01	148.78	28.9
Three Rivers	St. Joseph	35.15	146.20	24.0
Trenton	Wayne	33.28	143.79	23.1
Whitehall	Muskegon	34.65	134.82	25.7
Villages				
Eau Claire	Berrien	37.20	149.31	24.9
Elkton	Huron	35.76	129.59	27.6
Romeo	Macomb	54.83	146.80	37.3

Source: Michigan Department of Treasury, computations made by CRC.

reimbursement mechanism over the years. However, it is not likely that the location of inventory remained static during that time period. Moreover, it is probable that some units that lost inventory continued to receive payments for revenues that would have declined as a result of migrating inventories. Likewise, other units that gained inventory were unable to avail themselves of additional state payments.

Several units received substantial payments per capita and the prospect of losing that revenue source created concern and resistance by these units. In FY 1998, 25 communities, mostly cities, received per capita payments of \$30 or more from this source (see Table 1). Fifteen of these units received more than one-fourth of their total revenue sharing from inventory reimbursement payments.

2. Relative Tax Effort

Each unit's payment was determined by computing its population weighted by the ratio of its local tax effort in mills divided by the local tax effort statewide. In most units the local tax effort is the local property tax rate; in 22 cities that levy a city income tax the millage equivalent of the resident tax collections was added to the calculation, and in Detroit the excise tax on utility payments was converted to mills as well.

It was argued that Relative Tax Effort (RTE) reflected needs in the community, ability to raise revenues to support services, and the willingness of residents to tax themselves to pay for their government. However, it was also argued that the RTE calculation encouraged higher taxes and an unfair redistribution of state revenues to high tax areas.

The criticism of the RTE formula that it encouraged increased taxes was probably exaggerated. Since the "revenue sharing match" per capita for each mill of tax levy was only about \$2.50 in the final year of the formula, and an average unit with taxable value per capita of \$20,000 would raise \$20.00 per mill per capita, for most units the state payment was probably a small inducement to raising taxes. However, for units with low tax bases per capita, increased mills were matched at effectively a higher percentage, although the same dollar amount. A unit with taxable value (TV) per capita of only \$10,000 would raise \$10.00 per mill per capita and would still receive \$2.50, effectively a 25 percent match. In FY1998, 136 units, only eight percent of all units had taxable value per capita of \$10,000 or less. While the prospect of increased state aid probably was considered as tax increases were being discussed by local unit legislative bodies, it seems unlikely that it would have been a controlling consideration in decisions to raise taxes.

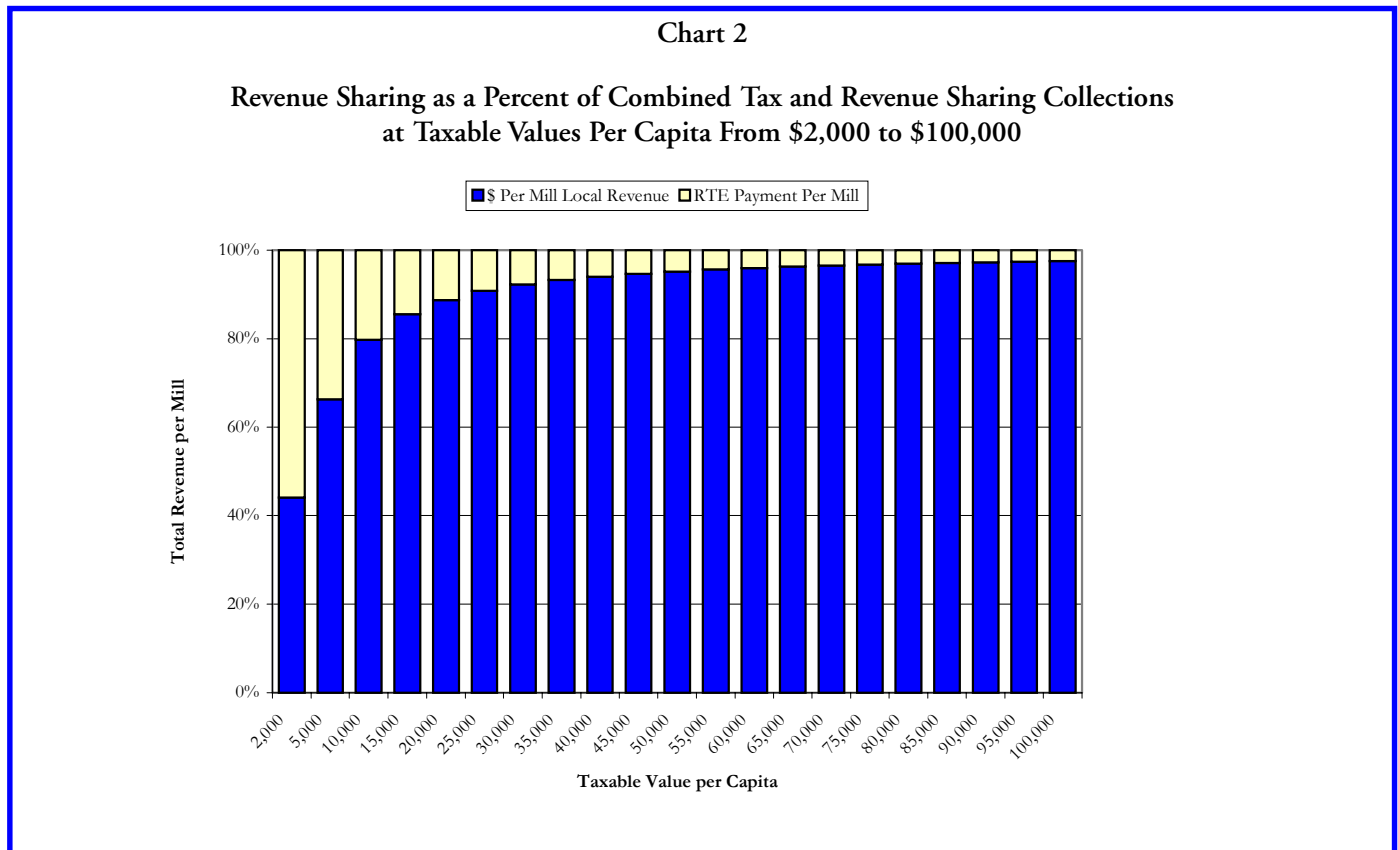


Chart 2 combines local tax yield with RTE payments as a percentage of total revenue per mill, illustrating the declining importance of RTE payments as TV per capita increases.

Because the constitutional portion of revenue sharing is distributed on a per capita basis, per capita payments became a benchmark to gauge the RTE formula and other proposed alternates. Each unit received nearly \$61 per capita constitutional payments in FY 1998. Compared with that per capita payment, the RTE formula generated very wide variations. A unit with one mill of local tax effort received about \$2.50 per capita, while Detroit, with approximately 92 mills of local tax effort received about \$230 per capita. More than 200 units levied one mill or less in FY1998. Almost all of them were townships.

Higher tax communities tend to be (1) communities with a more extensive array of services, (2) cities and villages (rather than townships), and (3) communities with lower taxable value per capita. Because of this, the RTE formula tended to provide a degree of equalization of revenue-raising capacity. However, if the principal objective of the formula was equalization, it had a fundamental flaw. The level of state support was entirely independent of any direct rela-

tionship to revenue raising capacity, as measured by taxable value per capita. Many examples exist of communities with virtually identical levels of tax effort with very large differences in taxable value per capita and correspondingly differing levels of tax revenue. Since the RTE formula has the effect of adding a constant amount per capita to the revenues available to two units with the same tax effort, the formula maintains the absolute difference in resources while narrowing the relative difference. **Table 2** illustrates the wide range of total revenue sharing plus local tax revenue resulting from large differences in taxable value and essentially the same local tax effort.

Despite the flaws in the two formulas, local units developed dependency on the revenues provided by the state. Formulas that would have the effect of changing payments in any substantial way were met with resistance from units that would lose and with enthusiasm from most units that would gain. Since the potential losses resulting from alternate formulas under consideration were concentrated primarily in urban communities in southeast Michigan and would adversely affect a minority of the local units and population in the state, political support for significant change was considerable.

Table 2
Relative Tax Effort Formula
Equalization Effects for Median Tax Rate Michigan Cities

		(1)	(2)	(3)	(4)	(5)	(6)
City	County	Local Tax Rate	Local Taxes Per Capita	RTE Payments Per Capita	RTE Plus Local Taxes	Ratio Local Taxes High to Low	Ratio RTE Plus Local Taxes High to Low
Crystal Falls	Iron	16.50	\$118.09	\$41.84	\$159.93	1.00	1.00
Montrose	Genesee	16.60	151.38	42.09	193.47	1.27	1.21
Mt. Pleasant	Isabella	16.40	169.80	41.59	211.39	1.45	1.32
Davison	Genesee	16.45	203.96	41.71	245.67	1.73	1.54
Adrian	Lenawee	16.53	209.27	41.92	251.19	1.77	1.57
Belleville	Wayne	16.60	245.62	42.09	287.71	2.07	1.80
Plainwell	Allegan	16.78	269.20	42.55	311.75	2.24	1.95
Rockwood	Wayne	16.74	275.47	42.45	317.92	2.30	1.99
Roseville	Macomb	16.75	285.76	42.48	328.24	2.38	2.05
Warren	Macomb	16.58	369.00	42.04	411.04	3.11	2.57
South Lyon	Oakland	16.79	372.19	42.58	414.77	3.10	2.59
St. Clair	St. Clair	16.62	445.98	42.15	488.13	3.75	3.05
Fraser	Macomb	16.50	451.20	41.84	493.04	3.82	3.08
Au Gres	Arenac	16.44	497.94	41.69	539.63	4.23	3.37
Marysville	St. Clair	16.81	522.97	42.63	565.60	4.34	3.54

Source: Michigan Department of Treasury, computations made by CRC.

III. The New Revenue Sharing Plan

The compromise reached in December 1998 included elements of the formulas proposed by individual members of the legislative task force. The task force itself, unable to reach agreement on changes that it could support, had essentially ceased operation in the summer of 1998. It was generally recognized that the large turnover in House members by the end of 1998 caused by term limits made

resolution of the changes in the formula under consideration essential or the House would likely have had to start the process of analysis and debate all over again.

The compromise that emerged from the legislature contained the following general elements:

A. New Formula for Units Other Than Detroit

A new mechanism containing three formulas was approved for all cities except Detroit and all villages and townships. The new formulas combine to change the payment shares significantly from the old two-part mechanism.

1. Ten-year Phase-in

In order to promote an orderly transition from the old to new formulas, a ten-year phase-in is included. Payments may not increase by more than eight percent from year to year. Amounts in excess of eight percent are distributed in a way that a floor is created for year-to-year declines or increases in total payments. One important exception to the eight percent increase limit provides that a unit whose 2000 census population increases by more than ten percent from the 1990 census is not subject to the eight percent growth limit for all years after FY 2000. From FY2001 to FY2006, the mechanism will likely prevent any year-to-year declines, providing the state permits the full amount of statutory revenues to be distributed and the Sales Tax revenue base grows at about four percent per year.

2. Freeze Detroit Allocation

Detroit's combined constitutional and statutory revenue sharing payments are frozen at \$333.9 million for fiscal years 1999 through 2006. In exchange for the protection from declines in payments resulting from census reductions and the new formulas, the city's personal Income Tax rate will be reduced by one-tenth of a percentage point per year from its 1998 rate of three percent to two percent. The rate on

non-residents working in the city will be reduced from 1.5 percent to one percent over the same period of time. The city also obtained legislation lowering the population threshold for its Income Tax rate and authorization to levy the Utility Users Excise Tax from 1,000,000 to 750,000. By freezing Detroit's payments, the growth the city would have received under the prior payment formulas is available to distribute to other units.

3. The New Formulas

Statutory revenues are subject to three separate distribution formulas with each formula operating on one-third of the revenue base. A detailed description of the formulas is contained in the appendix.

a. Unit Type Population Weighting

This component is based on the contention that service delivery costs are a function of the type of unit and population size within a given unit type. Cities are regarded as the most complex unit type, followed by villages and townships. A separate table of weights is used for each type of unit and the weights are different for different intervals of population size (see **Figure 2**). Weights increase as population increases and weights are progressively higher for a given population as the unit type moves from township to village to city. A unit's population is multiplied by a weight ranging from 1.0 (small township) to 7.46 (City of Grand Rapids).

The relationship between weights for different types of units at the same population size is illustrated in **Chart 3**.

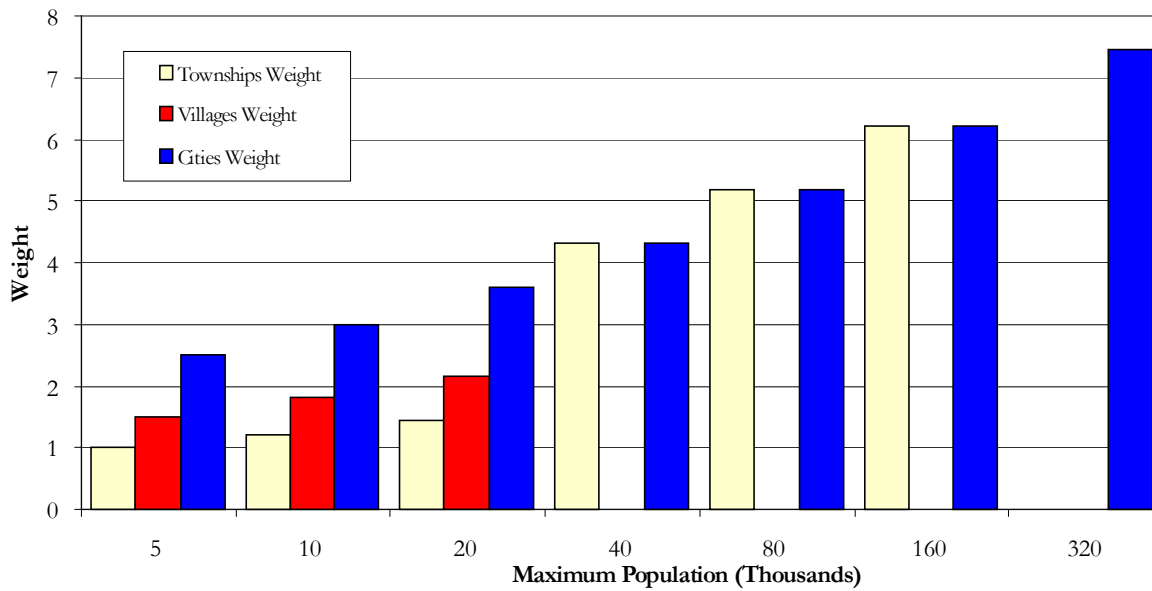
Figure 2

Unit Type Population Weights

Population		Weight	
Cities			
5,000 or less	2.50	Villages	
More than 5,000 but less than 10,001	3.00	5,000 or less	1.50
More than 10,000 but less than 20,001	3.60	More than 5,000 but less than 10,001	1.80
More than 20,000 but less than 40,001	4.32	More than 10,000	2.16
More than 40,000 but less than 80,001	5.18	Townships	
More than 80,000 but less than 160,001	6.22	5,000 or less	1.00
More than 160,000 but less than 320,001	7.46	More than 5,000 but less than 10,001	1.20
(The following weights are in the statute, but no units fall into the intervals)			
More than 320,000 but less than 640,001	8.96	More than 10,000 but less than 20,001	1.44
More than 640,000	10.75	More than 20,000 but less than 40,001	4.32
		More than 40,000 but less than 80,001	5.18
		More than 80,000	6.22

Chart 3

Unit Type Population Formula Weights

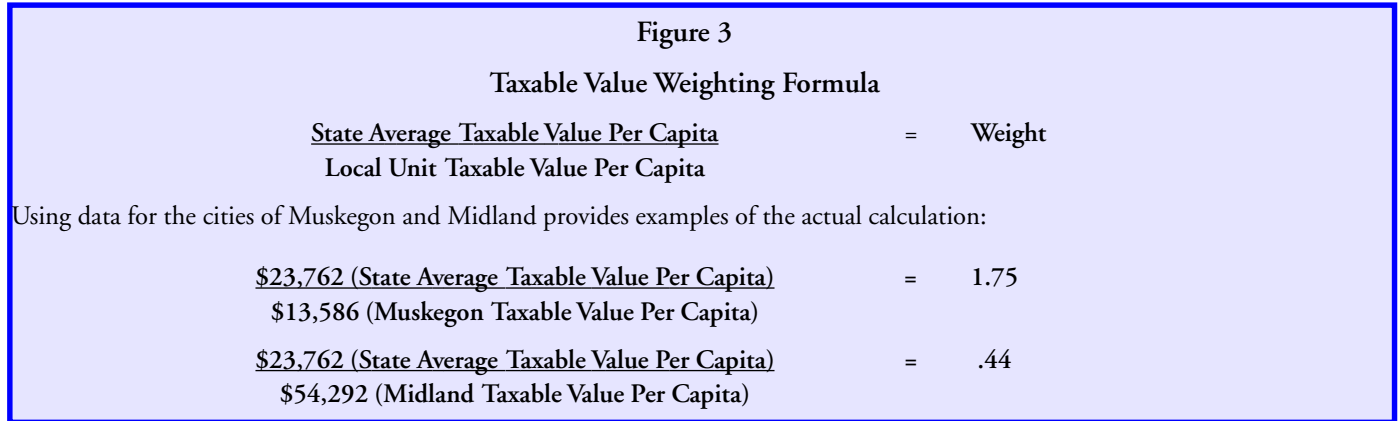


b. Taxable Value Per Capita Weighting

This component is intended to provide greater state support to units with smaller per capita tax bases. The state average TV per capita is divided by each unit’s TV per capita

and the result is multiplied by the unit’s population to obtain the unit’s weighted population (see Figure 3).

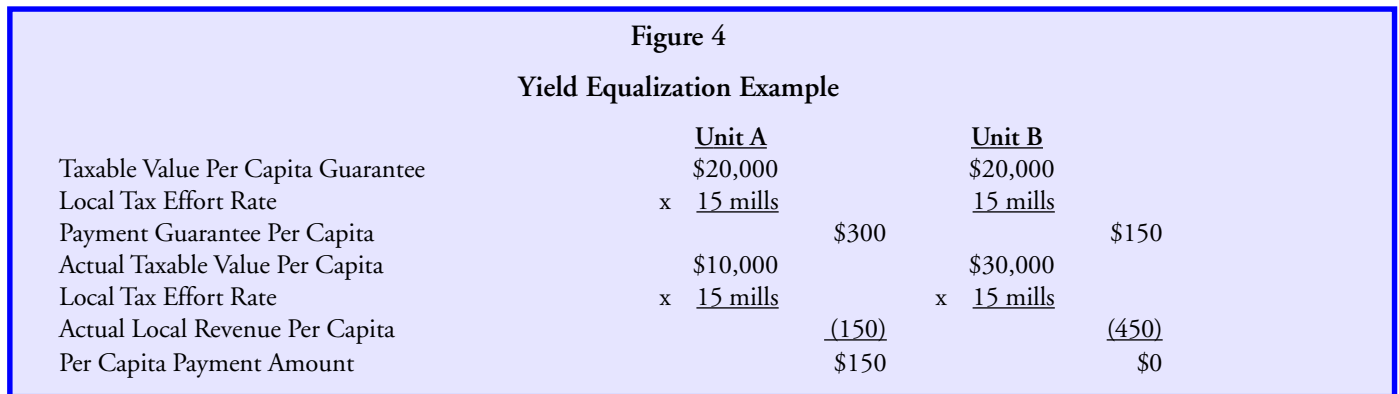
By providing higher payments to units with lower TV per capita, the formula adjusts for revenue raising capacity.



c. Yield Equalization

This component is intended to create a minimum guarantee on combined state and local revenue per mill of tax levy. The amount necessary to guarantee the total revenue proceeds (tax collections plus state payment) from each mill of local tax effort up to a maximum of 20 mills is computed. The guarantee is expressed in terms of a taxable value per capita (approximately \$22,000 for FY2000 payments) that would pay out the entire amount of statutory revenues. The calculation is the local tax effort in mills (up to a maximum

of 20) times the difference between the guarantee and the actual taxable value per capita for the unit times the unit’s population. The formula payment amount is one-third of the amount computed by this taxable value guarantee calculation. Only units with taxable values per capita less than the guarantee amount (about \$22,000) receive payment under this formula. This component has the effect of creating a partial floor under the total state and local revenue yield for each mill levied, up to the maximum guarantee of 20 mills. The formula is illustrated by Figure 4.



d. Total New Statutory Formula Payment Amount

The three formula payment amounts are added to derive the total payment amount.

e. The Ten-year Phase In

Beginning in FY1999, for each local unit, the shares of to-

tal statutory revenue sharing are determined for the FY1998 actual payments and the fiscal year for which the distribution is being made. In FY1999, 90 percent of the distribution is based on the FY1998 shares and ten percent is based on the FY1999 shares. In FY2000, 80 percent of the distribution is based on FY1998 shares and 20 percent on FY2000 shares. This calculation progression continues throughout

the statutory life of the program until FY2007. A unit's preliminary statutory allocation is determined by adding the two amounts, based on old and new formulas, together. The unit's constitutional payment is added to the preliminary statutory payment and any amount exceeding an eight-percent increase from the prior year is subtracted from the total unit payment. The amounts in excess of eight percent increases are distributed to units so that a uniform floor in

the percent decrease or increase is created.

Beginning in FY2001, the 2000 census population counts are used for the calculations for the new formulas. Any unit whose population increases by ten percent or more from census to census is not subject to the eight-percent increase limit for FY2001 and years after.

B. Generalizing the Effects of the Plan

The effect of the phase-in of three formulas, the phase-out of two formulas (actually three if the FY 1998 revenue growth distributed on a per capita basis is included), and the continuation of the constitutional formula is a six-part allocation mechanism, making any generalization of the overall effects difficult. Complicating the analysis is the occurrence of the 2000 census early in the phase-in period. New population counts would have caused significant changes in both statutory and constitutional payments even if the statutory formulas had not changed. If significant changes in payments for particular units occur between fiscal years 2000 and 2001, they will more likely be caused by the population changes than the new formulas.

A way to isolate the effects of the new formulas from other sources of change is to compare the shares of the statutory payments in the final year of the old formulas with the combined payment shares with the new formulas using the 1990 population counts for both calculations. The result of such a calculation, in effect, abstracts the revenue growth, population change, and eight-percent growth limit factors from the analysis and produces a comparison of the final shares each community would receive if the new formulas were fully implemented.

There is one further important complication in this approach to the analysis. While it permits comparisons under both the old and new formulas, the effect of removing Detroit from the statutory formulas and freezing the city's overall payment amount, in effect, redirects the revenue growth Detroit would have received to the rest of the units in the state. The total amount distributed to the remaining units is about \$13 million higher in FY2000 and by FY2007 that additional amount to be distributed will have grown to more than \$100 million. Over the life of the act, assuming a four percent annual increase in the revenue sharing base, total payments to units other than Detroit will increase by more than five percent per year and statutory payment increases will average about seven percent per year. The impact is substantial; any unit with a drop in statutory formula share of 20 percent or less finds its loss of share more than offset by the increase in distributable revenues.

The analysis that follows concentrates on the singular effects of the new formulas on distribution shares. But it is important to keep in mind that, if the effect of increased revenues is factored into the analysis, the number of units in the winners' category increases from 1,263 to about 1,400. Only about 375 units are likely to receive less revenue sharing as a result of the change in the program than they would have received.

Figure 5

The Revenue Sharing Calculator

The complexities of the new formulas and the difficulties presented to any unit attempting to factor the 2000 census into longer term projections argues for a statewide projection tool that bridges the pre and post census period. Citizens Research Council, with financial support from the Michigan Municipal League, developed a calculator that may be accessed on the CRC website. The calculator is based on a statewide projection model that incorporates actual data for FY1998 and FY1999 payments, taxable value, taxes, and 1990 population. Year 2000 population projections were developed by the state Department of Management and Budget. Visitors to the calculator may substitute their own 2000 population figure for a unit or run the calculator several times using a range of population figures. The calculator produces statutory, constitutional, and total payment figures for state fiscal years 1998 through 2006. The calculator is updated periodically to reflect significant events such as the Governor's Executive Budget proposal, legislative appropriations, and the availability of basic data on local unit tax collections and taxable value. The Calculator address is:

<http://calculator.crcmich.org>

IV. The Formula Effects Isolated

In the aggregate, townships and villages benefit and cities lose under the new formulas. Approximately three-fourths of villages and townships are winners, while only about two-

fifths of cities gain payment shares. Table 3 summarizes the numbers of winners and losers by unit type and provides the percentages in each category.

Table 3
Summary of Winners and Losers

	Winners	Percent	Losers	Percent	Totals
Cities	107	39.3	165	60.7	272
Villages	192	73.8	68	26.2	260
Townships	<u>964</u>	77.7	<u>276</u>	22.3	<u>1,240</u>
Totals	1,263	71.3	509	28.7	1,772

The overall summary of winners and losers confirms the general impression reported at the time the changes were enacted. However, many units in the favored groups, townships and villages, are disadvantaged by the formulas, and 40 percent of cities gain. In order to explore the formula

effects in more detail and identify the characteristics of units gaining and losing, two groups of specific units were selected for review: the most populous units and a representative group of smaller cities, villages, and townships.

A. Michigan’s Most Populous Units

The first group is composed of relatively large cities and townships. Presented in Table 4 are data for the largest 100 units (excluding Detroit) based on 1990 population and/or projected 2000 population. Most units fall into both categories, with eight included in the top 104 units in only one of the two years. These larger units tend to face a different set of service delivery demands than smaller units and tend to levy higher tax rates than smaller units.

The analysis measures the change in payments that would occur if the new statutory changes were to occur in total in FY1998 in order to assess the effect of the new formulas

without any changes in the amount of revenue distributed. Also included are the new shares in total revenue sharing, statutory plus constitutional, again *assuming the statutory changes were implemented all at once*. The addition of the constitutional payments to the measure narrows the range of changes in payment shares. Finally, the effect of the 2000 census counts is introduced into the analysis. The dynamics of population change, formula changes, and revenue growth are illustrated by the analysis and the generalized conclusions drawn from the analysis should apply to units with similar patterns of characteristics.

Table 4
Summary Individual Unit Statistics for Michigan's 100 Most Populous Units in 1990 or 2000
Ranked by New Statutory Formula Gain/Loss

	UNIT	Unit Type	COUNTY	1990 Population	Statutory Formula Percent Difference	Total Revenue Sharing Percent Difference	1990/2000 Population Percent Change	FY1999 Local Tax Effort	FY1999 Taxable Value Per Capita (1990 Pop)	Projected FY98/FY06 Tot Payment Percent Change
1	Summit	T	Jackson	21,130	539.8	42.4	9.3	0.88	17,170	79.6
2	Georgetown	T	Ottawa	32,672	278.7	29.6	29.4	2.50	24,616	150.7
3	Bedford	T	Monroe	23,748	231.5	28.2	19.9	2.10	23,339	118.2
4	Mt Morris	T	Genesee	25,198	152.5	52.0	0.9	11.22	10,614	79.0
5	Gaines	T	Kent	14,533	133.9	13.8	35.8	1.61	24,499	125.0
6	Genesee	T	Genesee	24,093	129.1	38.3	(1.8)	8.23	12,911	78.1
7	Plainfield	T	Kent	24,946	118.2	19.8	18.6	3.13	25,969	101.3
8	East Lansing	C	Ingham	51,065	99.2	46.1	(10.2)	19.56	11,288	77.9
9	Mt Pleasant	C	Isabella	23,178	88.9	39.5	0.5	16.40	11,271	77.4
10	Inkster	C	Wayne	30,772	81.7	45.2	0.3	29.63	7,697	77.3
11	Macomb	T	Macomb	22,714	77.4	13.3	110.5	5.05	45,289	258.4
12	Commerce	T	Oakland	22,156	76.5	12.9	31.9	3.45	50,492	109.7
13	Saginaw	T	Saginaw	37,684	56.0	12.6	3.6	5.41	24,217	65.5
14	Burton	C	Genesee	27,437	54.1	17.0	(1.0)	8.74	17,281	69.2
15	Hazel Park	C	Oakland	20,051	53.7	29.1	(3.2)	24.13	10,416	76.1
16	Brighton	T	Livingston	14,815	53.0	6.1	22.6	2.18	40,028	82.0
17	Blackman	T	Jackson	17,112	47.2	8.8	1.6	2.96	19,687	57.5
18	Flint	T	Genesee	34,072	43.1	10.4	(2.0)	6.50	24,003	53.7
19	Byron	T	Kent	13,235	40.8	5.7	36.1	2.82	31,475	104.6
20	Eastpointe	C	Macomb	35,283	38.4	17.9	(5.2)	20.47	15,086	67.3
21	White Lake	T	Oakland	22,500	37.7	8.8	21.5	6.46	29,554	89.7
22	Hamburg	T	Livingston	12,948	36.7	4.6	45.1	3.36	40,843	115.3
23	Garden City	C	Wayne	31,846	36.4	16.5	2.4	17.87	15,098	75.5
24	Muskegon	C	Muskegon	38,492	34.2	17.3	(3.0)	19.80	13,586	70.5
25	Adrian	C	Lenawee	22,026	32.2	15.1	(0.6)	16.05	14,187	74.1
26	Harrison	T	Macomb	24,685	30.8	7.9	3.0	6.21	24,797	59.2
27	Lincoln Park	C	Wayne	41,832	30.3	16.5	0.2	26.63	12,730	74.9
28	Westland	C	Wayne	84,583	30.2	12.6	1.4	15.24	17,526	75.5
29	Clinton	T	Macomb	85,866	30.0	9.3	14.7	11.20	22,899	96.8
30	Ypsilanti	C	Washtenaw	24,846	29.5	16.8	(9.6)	26.33	11,150	57.5
31	Chesterfield	T	Macomb	25,905	25.1	6.1	36.3	7.85	32,893	107.9
32	Dearborn Heights	C	Wayne	60,838	24.8	10.5	(2.2)	18.88	17,729	62.8
33	Benton	T	Berrien	17,163	24.0	8.8	(9.0)	10.84	17,028	42.1
34	Bay City	C	Bay	38,849	22.2	12.7	(11.2)	24.07	11,657	48.9
35	Kalamazoo	T	Kalamazoo	20,976	21.1	9.2	(1.4)	13.41	15,709	64.2
36	Grand Rapids	C	Kent	188,627	18.6	9.2	(3.2)	21.65	17,084	62.8
37	Delhi	T	Ingham	19,190	18.4	4.9	12.1	8.22	21,273	90.3
38	Flint	C	Genesee	140,690	15.4	9.4	(8.4)	27.90	11,580	54.4
39	West Bloomfield	T	Oakland	54,516	13.7	3.7	14.2	8.11	47,803	70.2
40	Kentwood	C	Kent	37,826	13.6	3.5	13.1	6.20	35,617	74.1
41	Grand Blanc	T	Genesee	25,392	13.0	3.6	10.9	7.03	27,737	65.2
42	Norton Shores	C	Muskegon	21,755	12.0	3.5	6.2	8.18	23,177	60.5
43	Orion	T	Oakland	21,019	11.2	2.7	44.4	6.15	53,985	112.5
44	Northville	T	Wayne	16,512	10.3	2.3	30.4	7.66	45,437	96.5
45	Marquette	C	Marquette	21,506	9.8	4.3	(13.5)	16.13	17,349	28.1
46	Saginaw	C	Saginaw	69,331	9.8	6.4	(10.5)	35.22	9,217	46.5
47	Jackson	C	Jackson	37,329	7.0	4.2	(7.6)	27.06	11,483	48.4
48	Meridian	T	Ingham	35,256	6.9	1.9	7.3	8.93	29,824	57.9
49	Bloomfield	T	Oakland	42,473	5.9	1.6	(0.4)	7.00	59,774	46.0
50	Delta	T	Eaton	26,129	5.1	1.4	16.8	5.98	32,165	71.6
51	Rochester Hills	C	Oakland	61,766	4.6	1.4	9.9	8.20	38,425	61.6
52	Taylor	C	Wayne	70,811	2.5	1.3	1.6	25.32	15,653	64.4
53	Ypsilanti	T	Washtenaw	45,307	(0.1)	(0.0)	2.0	11.64	19,795	57.1
54	Independence	T	Oakland	23,717	(0.8)	(0.2)	33.8	7.80	36,756	93.6
55	Lansing	C	Ingham/Eaton	127,321	(2.1)	(1.3)	0.3	30.61	13,977	59.9

Table 4
Summary Individual Unit Statistics for Michigan's 100 Most Populous Units in 1990 or 2000
Ranked by New Statutory Formula Gain/Loss (continued)

	UNIT	Unit Type	COUNTY	1990 Population	Statutory Formula Percent Difference	Total Revenue Sharing Percent Difference	1990/2000 Population Percent Change	FY1999 Local Tax Effort	FY1999 Taxable Value Per Capita (1990 Pop)	Projected FY98/FY06 Tot Payment Percent Change
56	Wyandotte	C	Wayne	30,938	(2.5)	(1.3)	2.5	21.69	15,863	62.1
57	Highland Park	C	Wayne	20,121	(2.9)	(2.1)	(6.6)	53.82	5,724	45.8
58	St Clair Shores	C	Macomb	68,107	(3.8)	(1.4)	(5.0)	12.83	20,511	41.6
59	Canton	T	Wayne	57,040	(4.0)	(1.3)	39.6	10.13	31,636	102.2
60	Shelby	T	Macomb	48,655	(4.7)	(1.5)	37.8	10.03	35,492	98.9
61	Hamtramck	C	Wayne	18,372	(4.7)	(3.3)	(3.8)	39.03	7,970	47.7
62	Waterford	T	Oakland	66,692	(5.0)	(1.7)	14.9	9.64	25,718	66.5
63	Kalamazoo	C	Kalamazoo	79,889	(8.3)	(4.8)	(6.7)	25.42	15,093	38.1
64	Roseville	C	Macomb	51,412	(9.5)	(4.4)	(1.7)	16.38	18,704	47.6
65	Highland	T	Oakland	17,941	(12.4)	(2.9)	11.6	5.68	25,343	76.6
66	Sterling Heights	C	Macomb	117,810	(12.5)	(4.8)	5.8	11.22	28,690	49.9
67	Holland	T	Ottawa	17,523	(13.6)	(3.8)	57.3	7.08	40,361	128.7
68	Oak Park	C	Oakland	30,468	(14.9)	(8.7)	(4.1)	26.78	15,080	39.3
69	Port Huron	C	St Clair	33,605	(16.3)	(9.3)	(5.2)	29.30	15,905	35.1
70	Berkley	C	Oakland	16,960	(18.2)	(7.7)	(3.2)	15.81	19,507	37.9
71	Frenchtown	T	Monroe	18,225	(18.5)	(4.9)	14.5	6.23	65,754	62.4
72	Farmington Hills	C	Oakland	74,614	(18.5)	(6.4)	7.3	11.09	41,143	54.4
73	Redford	T	Wayne	54,387	(20.4)	(10.3)	1.1	15.59	18,216	48.0
74	Pittsfield	T	Washtenaw	17,123	(20.5)	(5.8)	49.4	6.97	49,560	110.6
75	Southgate	C	Wayne	30,684	(21.7)	(10.8)	6.3	21.86	18,665	58.0
76	Livonia	C	Wayne	100,850	(23.7)	(9.5)	0.2	10.36	36,023	36.7
77	Plymouth	T	Wayne	23,423	(24.7)	(8.0)	24.8	5.45	51,305	67.9
78	Wyoming	C	Kent	63,891	(26.4)	(10.8)	9.4	11.85	23,522	53.4
79	Vanburen	T	Wayne	21,010	(26.7)	(10.3)	26.5	9.94	23,217	89.6
80	Royal Oak	C	Oakland	65,410	(28.5)	(11.9)	(3.0)	13.60	22,882	29.5
81	Troy	C	Oakland	72,884	(29.2)	(10.6)	9.2	9.81	54,813	45.1
82	Mt Clemens	C	Macomb	17,941	(29.7)	(17.3)	(5.6)	23.87	16,630	26.5
83	Portage	C	Kalamazoo	41,042	(31.5)	(12.7)	7.4	11.60	31,655	41.4
84	Ferndale	C	Oakland	25,084	(32.3)	(20.5)	(3.5)	29.93	15,386	26.1
85	Walker	C	Kent	17,279	(33.2)	(11.4)	19.0	10.81	35,346	60.9
86	Novi	C	Oakland	32,998	(34.4)	(12.0)	40.9	10.76	54,446	89.6
87	Battle Creek	C	Calhoun	53,516	(34.4)	(19.2)	0.8	24.83	18,704	33.6
88	Ann Arbor	C	Washtenaw	109,472	(40.0)	(19.2)	0.1	19.02	27,035	26.6
89	Pontiac	C	Oakland	70,177	(41.3)	(30.4)	(3.9)	42.23	12,118	25.9
90	Midland	C	Midland/Bay	38,016	(44.0)	(17.0)	5.4	11.62	54,292	36.8
91	Warren	C	Macomb	144,864	(44.3)	(22.5)	(3.5)	16.58	24,134	26.3
92	Allen Park	C	Wayne	30,886	(47.9)	(22.2)	1.3	16.69	24,761	26.5
93	Holland	C	Ottawa/Allegan	30,745	(49.0)	(22.8)	8.1	15.79	25,533	29.9
94	Southfield	C	Oakland	75,703	(49.2)	(23.0)	(1.7)	16.68	35,734	26.4
95	Dearborn	C	Wayne	89,286	(51.8)	(26.3)	3.8	15.71	40,796	26.1
96	Auburn Hills	C	Oakland	17,026	(52.5)	(20.3)	14.4	12.40	59,688	35.9
97	Monroe	C	Monroe	22,838	(55.1)	(26.1)	(5.5)	14.48	33,378	26.2
98	Romulus	C	Wayne	22,897	(55.4)	(26.9)	9.9	12.98	29,485	27.0
99	Madison Heights	C	Oakland	32,196	(57.9)	(29.2)	(2.0)	17.37	27,613	25.9
100	Grosse Pt Woods	C	Wayne	17,715	(58.4)	(26.8)	1.0	19.95	34,449	26.2
101	Wayne	C	Wayne	19,899	(59.7)	(34.5)	4.1	20.08	20,212	30.0
102	Birmingham	C	Oakland	19,997	(62.7)	(28.2)	(1.1)	15.59	56,462	26.2
103	Brownstown	T	Wayne	18,811	(63.1)	(33.7)	24.1	11.34	22,149	51.2
104	Trenton	C	Wayne	20,586	(70.3)	(40.8)	5.0	19.33	31,554	25.9
STATE TOTALS (Excluding Detroit)				8,243,772			8.1	10.13	25,945	59.6

In the aggregate, the 104 units appear to be fairly representative of the total state, although rural areas are clearly underrepresented. Table 5 provides summary statistics for the units compared with the state totals and averages. The units make up just over half of the 1990 population and will slip slightly in the share of the 2000 population. About 69.1 percent of the old statutory formulas payments went to these units and the new share, if the new formulas were fully implemented at 1990 populations, would slip to 65.6 percent of the state totals. When constitutional payments are factored in, the old formula shares are 59.5 percent and the new formula shares are 58.1 percent. The taxable value per capita for the units is 98 percent of the overall state average and the local tax effort, not surprisingly, is about one-third above the state average.

Attempts to identify strong patterns or associations between a unit's status as a winner or loser under the new statutory formulas have yielded mixed results. Of the 104 units in the group, 52 are winners and 52 are losers. Losses of more than 20 percent are reflected in the shares of 32 units, while 35 units gain more than 20 percent.

1. Winners and Losers

The ranges in the projected changes of the winners and losers among the individual units are very broad. The following represent the extremes in changes in shares of payments and the impact of the 2000 census:

The largest increase in the statutory share among these units is Summit Township in Jackson County, an increase of 540 percent. Summit Township has the lowest tax effort of the units in the analysis (.88 mills) and relatively low taxable value per capita (\$17,170). The largest reduction in share occurs in the City of Trenton in Wayne County, dropping by 70 percent. Trenton's tax effort is relatively high (19.33 mills) and its taxable value per capita is also relatively high (\$31,554). It receives no payment under the yield equalization provision.

After factoring in the constitutional per capita payments, the largest increase in share occurs in Mt. Morris Township in Genesee County, an increase of 52 percent. Mount Morris' local tax effort is about 10 percent above the state average (11.22 mills) and its taxable value per capita is about 40 percent of the state average (\$10,614). The largest decrease occurs in the City of Trenton, a decline of 41 percent.

Trenton's situation is affected significantly by the loss of inventory reimbursement payments. In FY1998, 23 percent of the city's total revenue sharing payments came from this source. Only 19 units had a higher percentage than Trenton and only two were in the populous unit group: Brownstown Township in Wayne County and the City of Pontiac in Oakland County. Both units also record large losses in payment shares. The unit with the highest share of total payments coming from inventory reimbursements was South Lyon, in Oakland County.

Table 5
Summary Total Statistics
100 Most Populous Units 1990 or 2000

	104 Units	State Totals (Excluding Detroit)	Percent of State Totals or Averages
1990 Population	4,342,710	8,243,772	52.7
2000 Population	4,576,034	8,913,663	51.3
Payment Share of Old Statutory Formulas			69.0
Payment Share of New Statutory Formulas			65.5
Old Total Payment Share			59.1
New Total Payment Share			57.8
Taxable Value Per Capita	\$25,341	\$25,945	97.7
Local Tax Effort (mills)	13.56	10.13	132.7
FY2006 Projected Statutory Payments (000)	\$371,364	\$575,416	64.5
FY2006 Projected Total Payments (000)	\$735,189	\$1,284,068	57.3

Note: Throughout the period beyond FY2001, revenues are assumed to grow four percent per year and all revenues earmarked by statute for distribution are assumed to be paid to local units.

South Lyon received nearly \$90 per capita in FY1998, 46 percent of its total payment base. Its share of statutory revenues drops nearly 60 percent.

2. How Units Gain

Generally, the new formulas favor units in the following ways:

Units with relatively low taxable values per capita receive added weight in the payment computation in two ways.

- First, through the ratio of the state average taxable value per capita divided by the units TV per capita (one third of the formula). A unit with TV per capita below the state average has its population weighted greater than one.
- Second, yield equalization payments (one third of the formula) are received if the taxable value per capita of a unit is below the guarantee level (about \$22,000 for FY2000). Up to a limit of 20 mills in the yield equalization calculation, units receive greater payments the greater the local tax effort.

In the unit type population weighting portion of the formula (one third of the formula), unit weights increase in intervals as population increases. For a specific population size, the weight is generally lowest for a township, higher for a village, and highest for a city. This pattern does not hold for townships with populations exceeding 20,000, which receive the same weight as cities with the same population.

Knowing the unit characteristics that result in greater payments does not necessarily enable one to predict how a unit will fare under the new formula relative to the old. There are only a few areas where winners or losers represent a high percentage of units with a given characteristic. The following summarize the findings for the most populous units:

- Winners and losers are divided fairly evenly by taxable value per capita until the TV per capita falls 40 percent or more below the state average. Two thirds of the units in that group are winners.
- For units with local tax effort (LTE) rates from ten mills

(the state average) to 16 mills (60 percent above the state average), losers outnumber winners by almost four to one. For units with LTE rates more than 20 percent below the state average (eight mills or lower), winners outnumber losers by more than five to one.

- Comparing units by unit type population weights reveals losers outnumbering winners for units with populations exceeding 80,000 by two to one, units with population between 20,000 and 40,000 showing winners exceeding losers by two to one, and about 60 percent of units below 20,000 losing payment shares.
- Finally, comparing units on a broad geographic basis yields a somewhat surprising result. As changes in the statutory mechanisms were debated in Lansing, it was alleged that most proposals would benefit the western part of the state vis-a-vis the southeastern part of the state. While winners outnumber losers in west Michigan by ten to six, 23 out of the 66 units in the seven-county southeastern area are also winners under the new formula. Interestingly, nine out of the ten units in the I-75 corridor of counties north of the Detroit area are winners and eight of the ten units in the central part of the state gain. (See Map 1.)

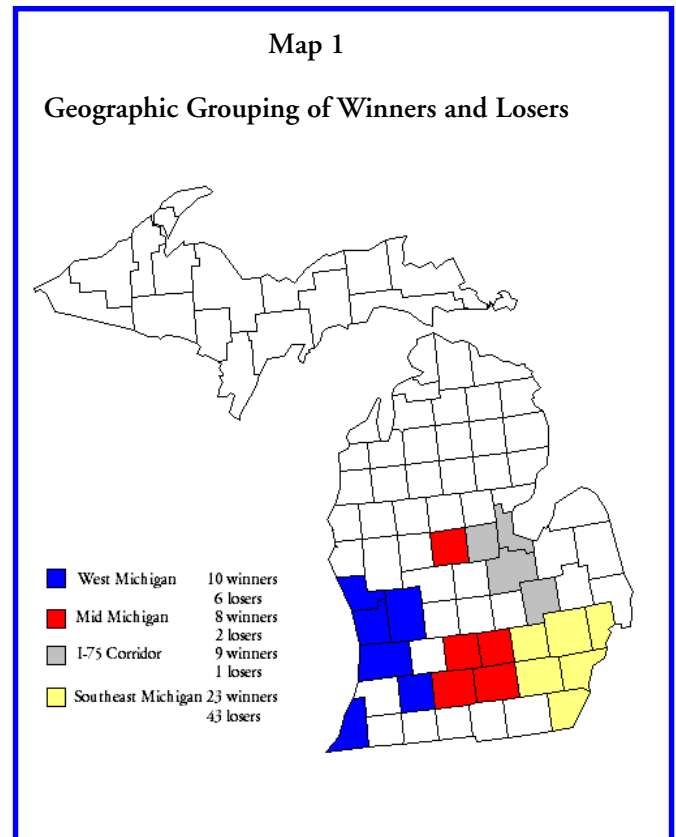


Table 6
Comparison of Statutory Share Changes
Cities with Similar Tax Effort in Different Population Intervals

City	County	Statutory Change	Taxable Value per Capita	Local Tax Effort
Grand Rapids	Kent	18.6	17,084	21.65
Battle Creek	Calhoun	(34.4)	18,704	24.83
Mt Clemens	Macomb	(29.7)	16,630	23.87
Southgate	Wayne	(21.7)	18,665	21.86
Wyandotte	Wayne	(2.5)	15,863	21.69

Since most of the old statutory formula was based on the number of mills of local tax effort (LTE), one would expect units with similar LTE rates and taxable value per capita to fare similarly when comparing old and new formula shares. However, the units in **Table 6** exhibit very different changes in statutory shares despite the similar LTE and TV per capita values.

The principal difference among these units is the unit type population weight each receives. This component affects one-third of the revenue distribution and Grand Rapids receives a weight of 7.46, 44 percent higher than Battle Creek, 73 percent higher than Southgate and Wyandotte, and 107 percent above Mt Clemens.

3. The 2000 Census

In FY2001, the impact of the 2000 census will dwarf any effects of the changes in formulas on unit payments. The magnitude of the census change for any unit is important for two reasons:

(1) All of the payment components, with the exception of residual shares of inventory reimbursement payments, are

population-driven. In FY2001, all of the constitutional payments will be based on 2000 population. Statutory payments will be based 70 percent on old formula shares and 30 percent will be based on new formula shares and 2000 population, reflecting the status of the ten-year phase in of the new formula.

(2) Complicating the situation is the provision that exempts from the yearly payment growth limit of eight percent any unit with population growth from 1990 to 2000 exceeding ten percent. Several hundred units will exceed the ten-percent growth threshold. The population growth for the state as a whole, excluding Detroit, is likely to exceed eight percent. CRC calculations indicate that about 1,000 of the nearly 1,800 units, serving 45 percent of the state population, excluding Detroit, will grow by more than ten percent.

Although the ten-percent provision will have the effect of removing funds from the pool used to create a floor under units who face significant losses in payments, the floor in payment changes is estimated at a 7.2 percent increase. Thus, in FY2001, no unit will receive less than a 7.2 percent increase in total payments regardless of its population change.

B. The Less Populous Units

In order to illustrate the effects of the new formulas on smaller units, 63 cities, villages and townships were selected that reflect variations in local tax effort, taxable value per capita, and population size. The population sizes were selected so units in each population interval of the unit-type population weighting formula are represented. The basic data for the units are included in **Table 7**. In addition to the measures of change in payment shares, population

change, local tax effort and taxable value per capita, the table includes information on the unit type population weight intervals and the relative levels of LTE and TV per capita of each unit. The LTE rates and TV per capita figures are grouped into low, medium, and high categories based on the distribution of these measures within each of the governmental unit types. A high LTE rate for a city is a very different number than a high LTE rate for a township.

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Table 7
Summary Individual Unit Statistics for Selected Less Populous Units

Unit	County	Population Interval	Local Tax Effort	Taxable Value Per Capita	Statutory Formula Percent Difference	Total Revenue Sharing Percent Difference	FY1999 Local Tax Effort	FY1999 Taxable Value Per Capita	Projected 1990/2000 Population Percent Change	FY98/06 Total Payment Percent Change
Galesburg	Kalamazoo	Less	Low	Low	139.8	44.4	9.23	10,188	(1.6)	78.3
Swartz Creek	Genesee		Low	Medium	(59.9)	(27.2)	7.65	24,655	(2.5)	26.2
Bloomfield Hills	Oakland	Than	Low	High	(41.7)	(10.2)	6.71	140,819	1.4	31.4
Manton	Wexford		Medium	Low	71.5	32.8	17.00	11,077	2.9	76.8
Gibraltar	Wayne	5,000	Medium	Medium	(66.0)	(33.6)	17.22	22,370	7.5	25.9
Gaylord	Otsego		Medium	High	(69.4)	(32.7)	16.76	37,874	21.6	29.3
Gobles	Van Buren	Weight = 2.50	High	Low	46.8	24.4	21.88	11,168	2.8	75.7
Newaygo	Newaygo		High	Medium	(66.3)	(34.2)	21.44	21,846	14.9	49.3
Saugatuck	Allegan		High	High	(76.2)	(37.0)	18.79	64,641	9.6	25.9
Hudsonville	Ottawa	5,000	Low	Medium	(36.2)	(13.4)	12.97	23,223	13.6	61.1
Saline	Washtenaw		Low	High	(76.1)	42.3	14.18	39,836	13.4	8.9
Belding	Ionia	to	Medium	Low	45.8	23.2	16.95	10,961	3.2	75.5
Centerline	Macomb		Medium	Medium	(75.9)	(45.9)	17.82	24,037	(4.1)	25.9
Northville	Oakland/Wayne	10,000	Medium	High	(65.5)	(30.6)	17.85	37,930	3.4	26.1
Ironwood	Gogebic		High	Low	65.1	35.5	25.38	8,770	(11.3)	75.2
Utica	Macomb	Weight = 3.00	High	Medium	(61.6)	(29.9)	22.05	24,964	(3.9)	25.9
Brighton	Livingston		High	High	(66.5)	(31.5)	18.77	39,185	16.5	25.5
Grandville	Kent		Low	Medium	(21.6)	(7.2)	9.16	26,440	5.6	43.6
Auburn Hills	Oakland	10,000	Low	High	(52.5)	(20.3)	12.40	59,688	14.4	35.9
Owosso	Shiawassee		Medium	Low	65.2	29.4	15.87	11,963	(5.6)	76.6
Traverse City	Gr Traverse/Leelanau	to	Medium	Medium	(54.3)	(24.8)	13.97	27,918	0.8	26.4
East Grand Rapids	Kent		Medium	High	(49.0)	(20.6)	15.74	30,206	(6.4)	26.7
Muskegon Heights	Muskegon	20,000	High	Low	69.7	39.2	25.07	7,837	(7.0)	76.7
River Rouge	Wayne		High	Medium	(82.8)	(57.5)	24.33	26,350	(5.8)	25.9
Grosse Pt Woods	Wayne	Weight = 3.60	High	High	(58.4)	(26.8)	19.95	34,449	1.0	26.2
Kaleva	Manistee	Less	Low	Low	219.9	50.3	8.00	10,616	(8.4)	78.0
Ortonville	Oakland		Low	Medium	(25.2)	(7.0)	8.00	22,923	15.8	68.3
Goodrich	Genesee	Than	Low	High	(49.8)	(15.2)	8.38	34,902	67.0	117.6
Woodland	Barry		Medium	Low	143.2	49.4	12.29	9,727	9.7	78.3
Lake Orion	Oakland	5,000	Medium	Medium	(54.9)	(21.1)	12.70	23,413	15.1	50.6
Elk Rapids	Antrim		Medium	High	(68.0)	(28.0)	12.79	33,873	22.0	35.4
Decatur	Van Buren	Weight = 3.60	High	Low	88.6	38.5	15.81	10,083	(1.3)	77.4
Dundee	Monroe		High	Medium	(62.1)	(26.7)	15.60	22,654	(1.4)	26.9
Chelsea	Washtenaw		High	High	(81.6)	(44.8)	16.82	33,682	15.1	6.2
Milford	Oakland	5,000 to 10,000 Weight = 1.80	Low	High	(66.6)	(29.5)	2.79	28,535	18.3	30.2
Beverly Hills	Oakland	Over 10,000 Weight = 2.16	Medium	Medium	(53.4)	(18.9)	13.96	36,603	(4.2)	27.1
Sheridan	Calhoun	Less	Low	Low	45.0	10.8	1.96	13,795	6.3	70.4
Adrian	Lenawee		Low	Medium	107.4	10.1	1.38	28,526	31.0	104.7
Penn	Cass	Than	Low	High	11.5	1.3	1.95	51,698	1.0	41.8
Skandia	Marquette		Medium	Low	169.1	33.4	4.34	11,538	(11.7)	58.7
Akron	Tuscola	5,000	Medium	Medium	(9.0)	(1.7)	4.26	29,529	8.0	50.9
Custer	Antrim		Medium	High	(41.0)	(6.7)	4.45	82,081	23.5	61.9
Sands	Marquette	Weight = 1.00	High	Low	143.4	33.2	6.70	12,269	(33.1)	30.7
Brevort	Mackinac		High	Medium	(37.5)	(9.2)	8.17	30,921	(1.4)	28.9
Sebewaing	Huron		High	High	(75.7)	(27.0)	7.03	60,405	4.6	26.6
Cooper	Kalamazoo	5,000	Low	Low	149.2	19.0	2.27	17,745	4.4	74.1
Algoma	Kent		Low	Medium	50.2	6.7	2.51	28,374	35.1	105.5
Ada	Kent	to	Low	High	(24.8)	(4.0)	2.99	61,924	28.7	74.2
Bedford	Calhoun		Medium	Low	189.1	33.7	4.17	12,265	1.7	78.3
St Joseph	Berrien	10,000	Medium	Medium	(6.1)	(1.2)	4.77	27,718	0.9	41.1
Clay	St Clair		Medium	High	(6.2)	(1.1)	4.42	34,717	5.7	47.6
Forsyth	Marquette	Weight = 1.20	High	Low	186.0	56.8	9.32	8,073	(41.9)	32.0
Northfield	Washtenaw		High	Medium	(46.6)	(13.9)	8.52	28,942	14.8	45.1
Milford	Oakland		High	High	(33.5)	(5.5)	6.19	79,556	33.0	77.1
Leoni	Jackson	10,000	Low	Low	126.9	18.9	2.15	16,902	5.6	76.8
Gaines	Kent		Low	Medium	133.9	13.8	1.61	24,499	35.8	125.0
Genoa	Livingston	to	Low	High	30.1	3.8	2.08	44,882	41.0	105.5
Emmett	Calhoun		Medium	Low	83.2	14.8	3.87	18,101	18.6	105.1
Monroe	Monroe	20,000	Medium	Medium	(6.6)	(1.6)	4.90	21,874	13.3	70.5
Green Oak	Livingston		Medium	High	15.9	2.2	3.51	45,752	29.0	85.7
Sumpter	Wayne	Weight = 1.44	High	Low	164.6	35.5	7.58	13,392	10.8	120.6
Mundy	Genesee		High	Medium	(22.5)	(5.9)	7.61	23,957	13.5	57.9

Of the 63 units in the analysis, 26 are winners while 37 are losers, using change in payment shares as the measure. When the changes in payment shares are examined in groupings based on the LTE and TV per capita measures, only one strong pattern emerges. All 19 units with low TV per capita experience significant increases in statutory payment shares and the increases average 110 percent. After adding the constitutional payment shares to the computation, the average increase is still a significant 31 percent. The emphasis given to TV per capita, which appears in two of the three formula components, translates to these gains for the low-value units. Of the 44 units with TV per capita categorized as medium or high, 37 lose payment shares while seven gain.

Since the old statutory formula was dominated by the LTE rate, it might be expected that low LTE rate units would experience payment share gains as the influence of LTE is lessened. However, of 20 units with low LTE, 10 are losers and 10 are winners. Eight of the 10 winners are townships whose LTE rates are all lower in absolute terms than any of the cities or villages in their respective low LTE category. This suggests that low LTE units are likely to be winners even if their TV per capita is high. Of the 1,143 total units with LTE rates at 5 mills or lower, 924 emerge as winners, and 900 of these are townships. The average TV per capita for these townships exceeds the overall state average and the range of TV per capita is \$5,200 to \$184,000.

C. What about Detroit?

The legislation approved in December 1998 provides an example of political compromise. Proponents of significant change generally used the per capita distribution in the constitutional portion of revenue sharing as a benchmark. As specific proposals were developed and measured against the RTE/Inventory Reimbursement mechanism, many argued that the large changes (generally reductions) reflected in a given proposal were too abrupt. Because Detroit had the largest RTE factor resulting in the city receiving about 45 percent of all the statutory payments, comparisons of formula alternatives inevitably singled out Detroit.

Those favoring the status quo or modest adjustments in the formulas generally argued that large changes would work undue hardships on the units with limited revenue raising capacity, as measured by low taxable value per capita and high tax effort. Weighting schemes giving consideration to relative property wealth and equalization of revenue raising capacity for a limited number of mills of tax levy were advanced. In reaction to a relatively complicated unit type/population size weighting structure proposed by a proponent of significant change, proponents of more modest change proposed a modified version. This version gave greater weights to larger units and recouped some of the potential shift in revenue sharing from more to less populous units.

Counter arguments emphasized that per capita distributions are really fairer, the old formula encouraged tax increases, and the changes would be even greater were the State to change to a straight per capita formula for statutory pay-

ments.

The process of reaching the final solution reflected significant give and take, involving key legislators and the Governor and special handling for the City of Detroit, potentially the biggest loser in most of the formulas under consideration. The final plan froze Detroit's total revenue sharing payments for fiscal years 1999 through 2006 at \$333.9 million and required that the city reduce its individual income tax rates on residents and non-residents by one-third over a ten-year period. This action protects Detroit from reductions resulting from the likely population decline in the 2000 census and the effects of a new statutory formula that would have reduced Detroit's share of the statutory revenue pie.

However, in determining whether Detroit benefited from the special treatment, it is necessary to compare the city's projected revenue sharing payments and taxpayer benefits with the revenue sharing formula that likely would have been approved had Detroit remained part of the formula calculations. The alternate possibilities include the Senate proposal and including Detroit in the plan that passed rather than freezing the city's payments. Although by no means certain, the Senate proposal was a more likely outcome than the bill that was approved with the city added to the formula. And it is unlikely that Detroit would have fared worse than the plan that had passed the Senate and been sent to the House for consideration.

Table 8 provides projections of Detroit's revenue sharing payments under current law and the bill that had received

Senate approval. Projections of the revenue reductions resulting from the phasing down of the individual income tax rates are also included. From the standpoint of the city budget only, the city will have less revenue over the period than if the Senate bill had passed. However, if the city and its taxpayers are viewed collectively, the new mechanism is beneficial vis-a-vis the Senate bill. Moreover, the provision limiting growth in payments to eight percent and redistrib-

uting the excess to units experiencing the largest relative losses would still be operative in FY2006, with Detroit receiving \$70 million in payments that would have provided protection against larger losses. Eventually this mechanism would run its course and the city's payments would have declined even farther. So the redistribution mechanism masks the eventual drop in the city's payments.

Table 8
Comparison of Alternative Revenue Sharing Programs Confronting Detroit

	Current Law			Senate Bill			
	Revenue Sharing Payments	Income Tax Reduction	Net Revenues to City	SB1181 Revenue Sharing	City Budget Difference From Current Law	Taxpayer Difference From Current Law	Collective Difference From Current Law
FY1998	331.8		331.8	331.8			
FY1999	333.9		333.9	306.8	(27.1)		(27.1)
FY2000	333.9	(11.6)	322.3	314.4	(7.9)	(11.6)	(19.5)
FY2001	333.9	(24.0)	309.9	318.3	8.4	(24.0)	(15.6)
FY2002	333.9	(37.1)	296.8	311.5	14.7	(37.1)	(22.4)
FY2003	333.9	(51.0)	282.9	305.6	22.7	(51.0)	(28.3)
FY2004	333.9	(65.8)	268.1	299.4	31.3	(65.8)	(34.5)
FY2005	333.9	(81.5)	252.4	292.4	40.0	(81.5)	(41.5)
FY2006	333.9	(98.2)	235.7	286.2	50.5	(98.2)	(47.7)

V. What Path Has Revenue Sharing Change Taken? Where Will It Go In The Future?

The new formulas resulted from a number of concerns and policy considerations:

- It was perceived by some that a formula that encouraged units to raise taxes should be eliminated.
- The mechanism to reimburse local units for lost inventory no longer was appropriate.
- Large units face more complex and expensive service demands than small units.
- At the same population level, the complexity and cost of different governmental forms declines from cities to villages to townships. This is often reflected by the less complex forms, depending on other units, usually the county, to provide services typically performed by cities.
- The state should somehow reflect revenue-raising ca-

capacity in the distribution mechanism.

- Revenue sharing is such an important component of local government finance that changes resulting from new formulas should be moderated.

The formulas that that Legislature approved arguably reflect these considerations. But in the final analysis, what has this meant so far and what will it mean in the future to the payments received by nearly 1,800 cities, villages, and townships in Michigan? The following material summarizes the path revenue sharing has traveled since the changes were first implemented and identifies some policy problems likely to confront the legislature as the sunset provision of the act approaches in 2007.

A. Fiscal Year 1999

1. Safety Mechanisms Moderate Change

In an effort to moderate change and protect units from reductions in payments, the first year of the new formulas contained the following safety mechanisms:

- No unit would receive less in FY1999 in combined statutory and constitutional payments than it received in FY1998. The provision was in effect for FY1999 only.
- The statutory payment components would be based 90 percent on a unit's percentage share of the FY1998 statutory payments and ten percent on the new statutory formulas.
- If the Legislature failed to appropriate the full amount of Sales Tax revenue called for in the revenue sharing statute, the shortfall would come entirely out of the new statutory formula component.
- The total amount a unit received could not exceed an eight-percent increase from the FY1998 total payment level. Amounts in excess of the eight-percent limit would be redistributed in a manner that created a uniform floor under the payment change percentage for all units.

2. The First Year's Experience

It is not surprising that the range of changes in total payments experienced by the local units was relatively narrow

when compared with the very large changes that the new formulas may ultimately bring. The first actual year of the new formula experience may be summarized as follows:

- The State failed to appropriate nearly \$18 million of revenues called for by the statutory percentages. This amounts to about five percent of the statutory base for units excluding Detroit and about two percent of the total payment base for these units. This entire shortfall came from the new formula component causing the new formula distribution to be reduced by more than half from a potential payment of \$34.8 million to \$17.1 million. The effect of the new formulas on the redistribution of revenues was lessened considerably as a result of this factor.
- The provision holding all units harmless from year-to-year reductions in payments *in the first year* provided protection to 54 units at a cost of less than \$400,000. Four cities received the majority of the payments: Ecorse, Pontiac, River Rouge, and Trenton.
- The distribution of change in payments was quite narrow when compared with the range that would have occurred had the new formulas been implemented without controls and phase-in of limits on increases. The payment increases ranged from no change (for 54 units) to seven percent. Without controls, the range of changes is estimated at minus 58 percent to an increase of 154 percent.

B. Fiscal Year 2000

1. Safety Mechanisms Continue

The following safety mechanisms continued from FY1999 into FY2000:

- The phase-in of statutory payment components continues and is based 80 percent on a unit's percentage share of the FY1998 statutory payments and 20 percent on the new statutory formulas.
- Any shortfall in the appropriation of sales tax revenue called for in the revenue sharing statute comes entirely out of the new statutory formula component.
- The total amount a unit received cannot exceed an eight percent increase and amounts in excess of the eight-percent limit are redistributed to create a floor under the payment change.

2. Projected Results

The following summarizes the FY2000 situation:

- The FY2000 appropriation was based on paying all of the sales tax percentage specified in statute. When the following components are combined, sufficient revenue growth is available to fund eight-percent increases in total statutory and constitutional payments for all cities, villages, and townships (except Detroit):
 - Approximately two percentage points of total

potential payments were not appropriated in FY1999. This revenue was included in the appropriation in FY2000.

- The growth that Detroit would have received had there been no change in revenue sharing (\$12.3 million) is available to distribute to the other units.
- The baseline growth in revenues reflected in the appropriations is 3.8 percent (subsequent revenue forecasts have raised the projected growth rate).
- Considerable redistribution between units occurs as the eight percent cap mechanism operates. Nearly 300 units which would receive double-digit increases with no cap are held at eight-percent increases. A total of 806 units are subject to the eight-percent cap and 969 benefit from redistributed revenues.
- At the end of the second year of the new formulas no unit will have received less than an eight-percent increase in payments from the FY1998 distributions.
- As units face the prospects of the 2000 census and its effect on allocations, units likely to experience population declines and who also lose payment share under the new formulas are positioned more favorably than if the overall payment change pattern had been even.

C. Fiscal Year 2001

1. The 2000 Census Begins to Affect Payments

The fiscal year begins on October 1, 2000 and the profile of projected changes is based on a complicated combination of projections and assumptions:

- The decennial Census of Population for 2000 defines the population data that will be used for revenue sharing calculations and allocations beginning in FY2001. Although the population totals will not be known and available to be used until about a year after the April 1, 2000 census date, the calculations will be adjusted back to the beginning of FY2001 (October 1, 2000).
- The state's population is expected to increase by about six percent and exclusive of Detroit by eight percent. Units failing to increase by at least as much as the overall state total (exclusive of Detroit) lose in their share of constitutional payments and generally lose in the new

formula portion of the statutory payments. However, the old formula shares, although declining in weight by ten percentage points each year, provide a temporary cushion to units with declining population shares.

2. Projected Results

Given the preceding considerations, the following summarizes the FY2001 outlook:

- The phase-in of statutory payment components is based 70 percent on a unit's percentage share of the FY1998 statutory payments and 30 percent on the new statutory formulas.
- Shortfalls in the appropriation of sales tax revenue called for in the revenue sharing statute continue to come entirely out of the new statutory formula component.
- Units with population increases from 1990 to 2000 of

ten percent or more are not subject to the eight-percent cap limitation mechanism in FY2001 or subsequent years. The population projections used in preparing this report have 914 of the 1,775 units (51 percent) exceeding the ten-percent threshold.

- For units whose 1990 to 2000 population change is less than a ten-percent increase or a decrease, the total amount received cannot exceed an eight-percent increase and amounts in excess of the eight-percent limit are redistributed as in previous years. Of the 1,775 units, 861 (49 percent) are projected to have their population change by less than a ten-percent increase.
- The appropriations for FY2001 reflect the consensus

revenue forecast and allocate all of the earmarked projected sales tax revenues. The year-to-year growth in total revenue sharing allocations for units except Detroit is 12.8 percent. This large increase pushes 471 of the units left in the eight percent cap category beyond the eight-percent growth limit and produces \$14 million for redistribution to units whose allocations would otherwise decline. Without the floor provided by this mechanism, year-to-year reductions as large as 26 percent would occur. Instead, the floor is estimated at a 7.2 percent increase. From the standpoint of units whose population decline is likely to be significant, a large amount of eight-percent cap funds couldn't come at a better time.

D. Three Years in Summary

Assuming approval of the Governor's budget proposal, after three years of phasing into the new formulas there are no significant dislocations or hardships experienced by the units subject to the formulas. The minimum increase in allocations over the three years is 15.8 percent, considerably in excess of the total rate of inflation for the period (about nine percent). The mechanisms in the new formulas designed to ease units into the new funding scheme have generally worked. However, the separation of units with growing population into two groups with an arbitrary cliff of ten percent has created some inequities and problems:

1. Problems with the Eight Percent Cap

The Legislature included the eight-percent cap mechanism to cushion payment reductions for units who are relative losers under the new scheme. However, units with slower growing or declining population were chosen to forgo some of their payments to assist the less fortunate units. Among those subject to the cap, 44 units have populations projected to decline between 1990 and 2000. While a decline in population, other things being equal, reduces revenue sharing payments, some units are such large winners under the new formula that the increase in formula share more than offsets a population decrease. An example is Benton Harbor whose population is projected to decline about eight

percent but whose statutory formula share increases 135 percent and total payment share increases by 86 percent.

The amounts of potential payments lost by some units are significant. The FY2001 projections include 13 units who collectively will lose \$5.7 million and individually are projected to lose more than \$250,000. Their calculated losses range, as a percentage of the FY2000 payments, between 1.7 percent and 13.3 percent. Data for these units is contained in Table 9.

2. Should Application of the Eight-Percent Cap Be Expanded?

The eight percent cap mechanism is only available to provide a floor under payment changes for units whose population change is less than a ten-percent increase. However, some units with population increases exceeding a ten-percent increase would qualify for payments under the mechanism, if the statute did not exclude them. It is likely that this result was not intended. Consideration should be given to amending the statute. In FY2001, 12 units are adversely affected by this provision. After FY2001, if the exclusion remains in place, 30 units are projected to experience year to year payment changes below the floor created by the eight-percent cap.

E. What Happens when The Sun Sets?

On June 30, 2007, the statutory formulas defining payments for cities, villages, and townships expire. Legislative action will be needed to determine future payment amounts. The possibilities are many, but a continuation of the cur-

rent law, with and without the eight-percent payment increase limit, is likely to receive consideration.

Continuation of the eight-percent mechanism would ex-

Table 9
Illustrative Losses for Selected Units from the Eight Percent Cap

Unit	County	Percent Payment Increase Without 8 Percent Cap	Payment Reduction Resulting From 8 Percent Cap	1990/2000 Population Change
Cities				
Benton Harbor	Berrien	18.9	269,158	(8.3)
Farmington Hills	Oakland	11.3	253,816	7.3
Garden City	Wayne	16.4	330,710	2.4
Grand Rapids	Kent	9.7	430,419	(3.2)
Inkster	Wayne	22.9	697,366	0.3
Lansing	Ingham/Eaton	12.0	840,563	0.3
Lincoln Park	Wayne	15.8	480,124	0.2
Mt Pleasant	Isabella	19.7	333,008	0.5
Rochester Hills	Oakland	13.6	332,357	9.9
Taylor	Wayne	12.6	472,664	1.6
Westland	Wayne	13.6	551,927	1.4
Wyoming	Kent	12.5	325,111	9.4
Township				
Mt Morris	Genesee	21.3	349,219	0.9

tend the period of controlled change for units that had not escaped the provision because their population increase exceeded ten percent. About \$14 million is projected to be redistributed to 138 units by the eight percent cap in FY2006. A total of 239 units contribute to maintaining a floor of a 1.4-percent increase. If the mechanism continues beyond the sunset of the act, it would take several years to eliminate all units from the cap. Approximately 20 units would likely extend beyond the 2010 census in terms of contributing to the cap fund.

An interesting possibility is the removal of the eight-percent limit. In order to analyze this possibility, projections of the payments in FY2008 were prepared under the assumption that new formula payment shares would be applied without any cushion provided by the eight percent mechanism. Approximately 100 units would experience drops in total payments in FY2008 compared with FY2006, despite increases in revenue to be distributed of ten percent over the two-year period. Some of the reductions would be very large. They arise from multiple factors:

- The new formulas significantly disadvantage a unit due to a specific set of factors that combine to reduce its

payment shares. A unit with (1) relatively high local tax effort (LTE), (2) taxable values higher than the threshold for yield equalization payments, and (3) relatively small population so its unit type population weight is low, would fall into this group.

- The unit received a significant percentage of its payments under the old formula from inventory reimbursement payments and no other factor rescues it from overall payment reductions when the eight percent protection is removed.

The 2000 population count reflects a very large drop in population in certain units, but the formula phase-in and eight-percent increase limit protection prevents payments from declining. A handful of units are likely to fall into this group. Such large population reductions are generally caused by significant shocks to their local economies from events such as the closure of K.I. Sawyer Air Force Base in Marquette County. Two townships in that county, Forsyth and Sands, have projected populations declines exceeding one-third.

Finally, 19 units in the model reflect reductions in total payments in FY2008 compared with FY1998. The major-

ity of the units have projected reductions in their population, explaining some or most of the reductions in payments. However, seven units reflect payment declines even though their population counts are projected to increase. Each of these units exhibits:

- Relatively heavy reliance on inventory reimbursement payments (from 15 percent to 37 percent of total revenue sharing payments in FY 1998) and
- TV per capita high enough to exclude the unit from participation in the yield equalization portion of the new distribution mechanism and cause the TV per capita weight to be low.

As the sunset of the current act nears, the Legislature will have to confront the issue of whether units will be permit-

ted to have their payments drop precipitously. The treatment of the City of Detroit will also have to be resolved. The starting point for this consideration will be the ending point of the current statute. The amounts received on a per capita basis for the statutory portion of the allocations will still exhibit large differences between units, although not as large as those when RTE was the principal distribution determinant. Perhaps a phase-in approach to a new set of formulas or continued use of the existing formulas could be considered. The final allocation amounts from the present act (before any sharp reductions had occurred) could be used as the starting point and a new phase-in period, perhaps with payment increase caps, would cushion any abrupt payment declines.

F. Effects of a Recession

1. A Moderate Downturn

Most of the analysis performed thus far has assumed that the future changes in revenue subject to distribution through the formulas will increase smoothly throughout future periods. The rates of increase used by state agencies in their projections have generally clustered around 4 percent and the CRC model assumes increases of 4 percent each year after FY2001. However, while the state and national economies are experiencing a record period of uninterrupted economic growth, the possibility of recession in the future still exists. In order to investigate the effect of a recession on the flow of payments, projections were prepared that assumed the following:

- The FY2001 appropriation is the beginning point for the multi-year projections.
- The FY2002 sales tax revenues grow by four percent from FY2001.

- In FY2003, no growth occurs in sale tax revenues (roughly the equivalent of a two-percent decline in inflation-adjusted revenues).
- In FY2004 and FY2005, growth occurs at an even rate sufficient to bring FY2005 sales tax revenues to exactly the level that would be achieved if annual four percent growth occurred from FY2001 to FY2005. This rate is slightly over six percent.
- The simulated recession, in summary, is of a one-year duration and takes two years of accelerated growth to return to a non-recession level of revenues and growth path.

a. Simulation Data

Table 10 provides a summary of total revenue sharing data used for the simulation.

Table 10

Projected Revenues for Distribution to Cities, Villages, and Townships
Total Revenue Sharing Allocations
Even Growth and Recession Simulation Comparison

Fiscal Year	Revenues No Recession (In Millions)	Percent Change From Prior Year	Revenues Recession in FY2003 (In Millions)	Percent Change From Prior Year
FY2001	\$1,365.2	7.7*	\$1,365.2	7.7*
FY2002	1,419.8	4.0	1,419.8	4.0
FY2003	1,476.6	4.0	1,419.8	0.0
FY2004	1,535.7	4.0	1,505.8	6.1
FY2005	1,597.1	4.0	1,597.1	6.1

*Calculated from FY2000 appropriation

b. Summary Financial Results

Eliminating the growth from FY2003 revenues produces 466 units whose projected payments would decline by an average (unweighted) of 2.6 percent; with a maximum decline of 7.3 percent (the floor created by the eight percent cap mechanism). A total of 1,309 units reflect increases averaging 2.6 percent with maximum increases of eight percent (the eight percent cap). In the two years following the year of

zero growth, the eight-percent cap mechanism produces more revenue to be distributed. The floor on the minimum increase is lifted from 1.9 percent and 1.7 percent in FY2004 and FY2005 in the even growth scenario to 7.3 percent and 6.8 percent respectively in the recession scenario. Table 11 provides yearly estimates of the amounts available to distribute from the eight-percent cap and the percentage change floors for each year under the two scenarios.

Table 11

Projected Revenues for Distribution to Cities, Villages, and Townships
Eight Percent Cap Mechanism
Even Growth and Recession Simulation Comparison

Fiscal Year	Even Growth Scenario		Recession Scenario	
	Eight Percent Cap Allocations (Millions)	Percentage Change Floor	Eight Percent Cap Allocations (Millions)	Percentage Change Floor
FY2003	\$11.0	1.7	\$4.7	(7.3)
FY2004	11.9	1.9	10.9	7.3
FY2005	13.1	1.7	17.7	6.8
FY2006	<u>14.4</u>	1.4	<u>16.3</u>	0.8
Totals	\$50.4		\$49.6	

c. Units Affected

With the larger amounts of eight-percent cap money to distribute, more units participate in both parts of the mechanism: giving and receiving. Table 12 provides data on both categories of units affected by the cap under the two scenarios.

d. Specific Examples

The projections for individual units reveal some surprising results. In the first year of the recession scenario, the reduction in revenues available from the eight-percent cap is significantly less than the even growth projections. Consequently, many units would suffer year-to-year declines in

Table 12
Number of Units Affected by Eight Percent Cap Mechanism
Even Growth and Recession Simulation Comparison

Fiscal Year	Even Growth Scenario		Recession Scenario	
	Units Contributing Eight Percent Cap Allocations	Units Receiving Eight Percent Cap Allocations	Units Contributing Eight Percent Cap Allocations	Units Receiving Eight Percent Cap Allocations
FY2000	806	969	806	969
FY2001	471	349	471	349
FY2002	379	241	379	241
FY2003	316	184	186	127
FY2004	284	162	481	296
FY2005	261	148	480	269
FY2006	239	137	364	170

payments, due to their status as overall losers under the new formulas and the increasing weight given to the new formulas under the phase-in mechanism. But following the recession year, many more units benefit from the eight-percent cap payments and their payments grow to a level exceeding the even growth projections by the second year following the recession. Two units were selected from the in-

dividual projections to illustrate the results. Table 13 provides projections for the City of River Rouge, a community depending heavily on the cap mechanism to protect against payment declines.

While River Rouge's projected payments under the recession scenario exceed the even growth projections in FY2005,

Table 13
Projected Revenue Sharing Allocations for the City of River Rouge
Total and Eight Percent Cap Payments
Even Growth and Recession Simulation Comparison

Fiscal Year	Even Growth Scenario		Recession Scenario	
	Eight Percent Cap Allocations (Thousands)	Total Allocations (Thousands)	Eight Percent Cap Allocations (Thousands)	Total Allocations (Thousands)
FY2002	\$456	\$2,658	\$456	\$2,658
FY2003	571	2,704	445	2,465
FY2004	714	2,756	655	2,643
FY2005	874	2,803	896	2,824
FY2006	1,050	2,841	1,056	2,846
Totals	\$3,665	\$13,762	\$3,508	\$13,436

the total projected payments for the five-year period are less with a recession than without one.

In the recession scenario, many additional units are brought into the category of contributors to the funds reallocated to units protected by the payment change floor. An example is the City of Grand Rapids. Grand Rapids gains in share from the new formulas and is likely to reflect a relatively

stable population when the 2000 census figures are available. Table 14 provides summary projections for Grand Rapids under the two scenarios.

The occurrence of a recession of the magnitude in the scenario is enough to push Grand Rapids into the category of contributing to the eight-percent payment pool. With post-recession payments growth limited to eight percent, Grand

Table 14

Projected Revenue Sharing Allocations for the City of Grand Rapids
Total and Eight Percent Cap Payment Reductions
Even Growth and Recession Simulation Comparison

Fiscal Year	Even Growth Scenario		Recession Scenario	
	Eight Percent Cap Reductions (Thousands)	Total Allocations (Thousands)	Eight Percent Cap Reductions (Thousands)	Total Allocations (Thousands)
FY2002	\$0	\$29,146	\$0	\$29,145
FY2003	0	30,956	0	29,346
FY2004	0	32,855	310	31,694
FY2005	0	34,847	616	34,229
FY2006	0	36,935	0	36,934
Totals	\$0	\$164,739	\$926	\$161,348

Rapids would be unable to recover the payment losses that are temporary for many other units. The payment losses are about \$3 million over the four-year period, with about one third resulting from the eight percent cap mechanism directly.

2. A Deeper Downturn?

While a recession resulting in flat sales tax revenues in nominal terms would present fiscal difficulties to the State and its local units, recessions of greater severity have occurred in the past. In order to test the sensitivity of payment changes, an assumption of a two percent year-to-year decline in sales tax revenues was introduced into the model. Instead of a floor of a 7.3 percent decline, the floor dropped to a 10.7 percent decline. In this scenario 56 units would fall to that floor and 169 units would experience payment declines ex-

ceeding five percent. A total of 620 units would still experience increases in payments and 85 units would contribute to the eight-percent cap mechanism.

At a four-percent decline in revenues, the floor would fall to a 15.3 percent decline and 32 units would be at that floor. Decreases of more than seven percent would affect 165 units. A total of 255 units would still experience payment increases and 61 of them would be at the eight-percent cap.

Unlike the effect of recessions on payments under the old formula when all units would experience approximately the same rate of change in payments as the overall revenue change, some units would continue to receive increases in their payments even in a severe recession. This is the result of the phase-in mechanisms that retard the growth of units benefiting from the formula and increases in their population.

G. Notch Effect of Ten Percent Population Gain

1. The General Problem

The ten-percent population growth provision creates a notch or cliff effect which is potentially dramatic for units very close to that threshold. Units whose payments could grow very rapidly because of increases in payment share, but whose population change is less than a ten-percent increase are affected by this situation.

2. Two Illustrations

Two units illustrate this phenomenon. Table 15 provides data for Kinross Township in Chippewa County. Its population projection in the model is an increase of 9.2 percent. By adding 35 persons to the 2000 projection, the township would gain over \$1.3 million spread over the five years FY2001 through FY2006. The two projected populations are essentially the same numbers statistically.

Table 15

Projected Revenue Sharing Allocations for Kinross Township
Effect of Ten Percent Population Threshold

	Model Projection	Percent Change	Adjusted Projection	Percent Change
1990 Population	4,575		4,575	
2000 Population	4,998	9.2	5,033	10.0
Difference			35	
	Payments (Thousands)	Percent Change	Payments (Thousands)	Percent Change
FY2000	\$374		\$374	
FY2001	404	8.0	531	41.8
FY2002	437	8.0	604	13.7
FY2003	472	8.0	685	13.4
FY2004	509	8.0	774	13.0
FY2005	550	8.0	871	12.5
FY2006	594	8.0	976	12.1
Totals	\$3,340		\$4,815	

On the other side of the ledger, **Table 16** displays data for the City of Coleman in Midland County. Its population is projected to increase 12.6 percent in the model. Adjusting

the populations down to just below a ten-percent increase results in significant reductions in projected revenue growth.

	Model Projection	Percent Change	Adjusted Projection	Percent Change
1990 Population	1,237		1,237	
2000 Population	1,393	12.6	1,359	9.9
Difference			(34)	
	Payments (Thousands)	Percent Change	Payments (Thousands)	Percent Change
FY2000	\$165	8.0	\$165	8.0
FY2001	224	35.7	179	8.0
FY2002	250	11.6	193	8.0
FY2003	279	11.3	208	8.0
FY2004	309	11.0	225	8.0
FY2005	342	10.7	243	8.0
FY2006	<u>378</u>	10.5	<u>262</u>	8.0
Totals	\$1,948		\$1,475	

VI. Issues for Further Analysis and Potential Action

The foregoing discussion has illustrated some of the idiosyncrasies of the new revenue sharing formulas. Despite the efforts to protect units from abrupt changes in their payments, especially declines, risks still exist that payments could decline significantly if certain conditions occur. The two greatest risks are recession and the sunset of the current legislation. Knowing in advance of the effect of sunset will permit policy options to be evaluated and deliberate action taken to continue revenue sharing, perhaps in modified form, in the future.

Unlike the past, when the rate of change in earmarked revenue essentially determined the rate of change in revenue sharing payments, a recession reflecting no change in nominal revenues would cause year-to-year declines in payments for many units. More severe downturns in Sales Tax collections could lead to very large declines in revenue sharing for a relatively small number of units. Being aware of this phenomenon should permit the State to provide advance notice to local units when revenue collections suffer from the effects of a recession.

Appendix: A Description of the New Revenue Statutory Formulas

In December 1998, the Michigan Legislature approved new distribution formulas for the statutory portion of the state’s revenue sharing program. The constitutional portion, which distributes 15 percent of the state’s Sales Tax at a 4 percent rate to cities, villages and townships on a per capita basis, remains unchanged.

The changes for counties were relatively insignificant. Inventory reimbursement payments are frozen at the state FY1998 level and the remaining revenues are distributed

on a per capita basis.

Beginning in FY1999, the City of Detroit’s total revenue sharing payments were frozen at \$333.9 million through FY2006. The new distribution scheme for the cities (except Detroit), villages, and townships is relatively complicated. It is based on a new three-part formula that produces population weights used to compute payments based on the unit’s weighted population. The three parts are as follows:

Part I –Variation in Taxable Value

The ratio of the statewide average taxable value per capita to the taxable value per capita for each unit is computed (a unit with taxable value below the state average receives a weight greater than one and units above the state average receive weights less than one). The weighted population for each unit is determined by multiplying its weight by its

population. Using the total state weighted population, a statewide per capita payment amount is computed to allocate one-third of the statutory revenues. Each unit receives an amount equal to its weighted population times the statewide per capita payment amount.

Part II — Unit Type/Population

The new statute includes a population weighting mechanism based on population size and the type of local unit as follows:

Cities	
Population	Weight
5,000 or less	2.50
More than 5,000 but less than 10,001	3.00
More than 10,000 but less than 20,001	3.60
More than 20,000 but less than 40,001	4.32
More than 40,000 but less than 80,001	5.18
More than 80,000 but less than 160,001	6.22
More than 160,000 but less than 320,001	7.46
More than 320,000 but less than 640,001	8.96
More than 640,000	10.75

Villages	
Population	Weight
Less than 5,000	1.50
More than 5,000 but less than 10,001	1.80
More than 10,000	2.16

Townships	
Population	Weight
5,000 or less	1.00
More than 5,000 but less than 10,001	1.20
More than 10,000 but less than 20,001	1.44
More than 20,000 but less than 40,001	4.32
More than 40,000 but less than 80,001	5.18
More than 80,000	6.22

Using the unit type population weights, the weighted population for each unit is determined by multiplying its weight by its population. Using the total state weighted population, a statewide per capita payment amount is computed to allocate one-third of the statutory revenues. Each unit receives an amount equal to its weighted population times the statewide per capita payment amount. A township with a population between 10,000 and 20,000 receives the higher weight for a city of the same size (3.60 instead of 1.44) if it provides 24-hour police and fire protection services and public water and sewer service to at least half its population.

Part III – Yield Equalization

The yield equalization portion is the state payment which guarantees that the total local and state proceeds from each equivalent mill of actual local levy yields at least a specified minimum amount. The millage used in the computation is the lesser of the actual equivalent mills levied by the unit or twenty mills. The amount per mill is computed as if all statutory revenues were distributed in this manner. The guarantee is projected to be approximately \$22,000 taxable

value per capita in FY2000. The actual payment amounts for each unit are one-third of the amount they would receive if the entire statutory base were distributed using the yield equalization formula, thus distributing one-third of the statutory revenues. Units with taxable value per capita exceeding the threshold receive no payment under this part of the formula.

Phase In and Growth Cap

If the new formula were implemented at a single point in time, very large year-to-year changes would be produced. In order to smooth out the year-to-year changes, the legislature included two provisions intended to promote more gradual change. The first, a ten-year phase in of the new formula specifies that in FY1999, ten percent of the statutory payment is based on the new formula and 90 percent on the percentage share the unit received of the FY 1998 statutory payments. Each year, an additional ten percentage points of payments are based on the new formula and the old formula share declines correspondingly.

In addition to phasing the implementation, the statute provides that the increase in total payments from statutory and constitutional revenues shall not exceed eight percent in any year. Amounts in excess of the eight percent threshold are paid to units in a way that creates a floor on the year-to-year increase (decrease) any unit receives in its total payments. However, when the 2000 census population counts begin to be used in FY2001, units with population increases exceeding ten percent from census to census are no longer subject to the eight-percent growth cap.

Appropriations versus Statutorily Required Allocation

Finally, if the state fails to appropriate and pay the full amount allocated for statutory revenue sharing in any year, the shortfall is subtracted from the amount distributed un-

der the new formula portion of the payment. In this situation, the old formula share payment is based on its share of the statutorily required allocation.

Key Assumptions-Growth in State Revenues after Distribution of \$333.9 million to Detroit

	Constitutional Payments (Millions)	Percent Change	Statutory Payments (Millions)	Percent Change	Total Payments (Millions)	Percent Change
FY1998	\$501.3		\$330.0		\$831.3	
FY1999	516.0	2.9	330.3	0.1	846.3	1.8
FY2000	546.1	5.8	368.2	11.5	914.3	8.0
FY2001	582.5	6.7	413.5	12.3	996.0	8.9
FY2002	605.8	4.0	443.4	7.2	1,049.2	5.3
FY2003	630.0	4.0	474.5	7.0	1,104.5	5.3
FY2004	655.2	4.0	506.8	6.8	1,162.0	5.2
FY2005	681.4	4.0	540.4	6.6	1,221.8	5.1
FY2006	708.7	4.0	575.4	6.5	1,284.1	5.1

Total Payments

Payments to cities, villages, and townships under the new statute comprise as many as five components:

- * Constitutional Per Capita
- * Percentage Share of Old Statutory Formula
- * Percentage Share of Variation in Taxable Value Component
- * Percentage Share of Unit Type/Population Component
- * Percentage Share of Yield Equalization Component (if any)

In addition, total payments may be subject to increases or decreases based on the eight percent cap mechanism.

Growth in State Revenues. The projections the revenue sharing calculator provides reflect certain assumptions about the growth in revenues that will be paid out by the State:

- * The appropriation for FY2001 distributes all statutory formula revenues based on state consensus revenue estimates and the Governor's FY2001 Executive Budget proposal.
- * After FY2001, baseline revenues grow by 4.0 percent per year through FY2006.
- * Constitutional per capita distributions are based on

baseline revenue estimates, with population estimates of the 2000 census used for per capita calculation beginning October 2001.

- * Detroit's total revenue sharing payments are frozen throughout the projection period in accordance with the revenue sharing statute. The growth Detroit would have received under the former law, had its distribution not been frozen, is available to increase the payments for the other local units beginning in FY1999. Consequently, statutory revenues available for distribution will grow an average of about seven percent per year after FY 2001. With constitutional revenues growing at 4.0 percent, the overall growth in revenues distributed to units other than Detroit exceeds 5 percent annually after FY2001.

It is assumed that statutory distributions will fully be paid out after FY2001. However, users are cautioned that the amount paid through the statutory formula could be less than the statutory formula amount of sales tax revenues. In order for this to occur, the State could either change the formula percentage of the sales tax or appropriate an amount less than formula percentage times the actual sales tax revenues.

Notes



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