Personal Property Tax

BACKGROUND

The property tax is Michigan's oldest form of taxation, dating back to at least 1893. Two types of property are taxed—*real* and *personal*—and both by state and local government. The tax rate on property in Michigan is determined by the number of mills levied, which is identical for real and personal property. For all jurisdictions in 1998, taxes on real property will generate approximately $9 billion and taxes on personal property about $1.4 billion.

Real Property

Real property generally is interpreted to include land plus the buildings and fixtures permanently attached to it. With Proposal A's passage in 1994, reliance on property taxes (for personal as well as real) was reduced for local governments and increased for state government (which now uses the revenue as a K–12 funding source).

Personal Property

Personal property generally is interpreted to be that not permanently affixed to land: e.g., equipment, furniture, tools, computers. In Michigan, only businesses pay the personal property tax (PPT); items for household use have been exempt since the 1930s. The exhibit shows that from 1985 to 1996 personal property taxes grew from $668 million to $1.2 billion—an 80 percent rise (24 percent when adjusted for inflation).

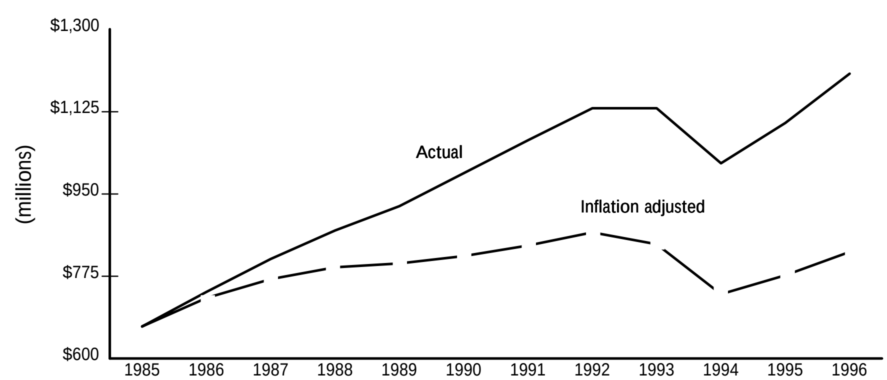
GLOSSARY

Mill
A monetary unit equal to 1/1000 *of a dollar;* millage *is the tax rate on property—the number of mills assessed against the property's taxable value.*

Personal property
Generally, items not attached to property; e.g., equipment, computers, furniture, tools.

Real property
Generally, items permanently attached to property; e.g., land, buildings, fixtures.

Estimated Michigan Personal Property Tax Collections, 1985–1996 (millions)



SOURCE: Senate Fiscal Agency.

- The state levies 6 mills on personal property, which is the level established for real property by Proposal A. In addition, there are state and local taxes that are tied to the PPT (i.e., state utilities tax and industrial facilities tax).
- The local levy varies from place to place, depending on what has been approved by local voters. Thus, if, in City A, 12 mills are levied on real property, 12 mills also are levied on the personal property of those who must pay it.

Reliance on personal property tax collections varies across the state. Some smaller rural counties raise less than $10 million in total annually from it, while in some larger counties it totals more than $5 billion annually. In some counties, the PPT represents less than 5 percent of total property value; in others it is significant—in Kalkaska and Midland counties, 59 percent and 63 percent, respectively (1996).

Cost to Business

Businesses pay both personal and real property taxes; of total business property taxes, nearly 38 percent is levied on personal property.

Proposal A substantially reduced the PPT. The average nonhomestead (includes business property) rate fell from 56.6 to 48.17 mills, about a 15 percent decline. Nevertheless, most statewide business associations list PPT repeal as a major legislative goal.

Other States

Thirty-five states levy a PPT, and in most the levy is similar to Michigan's. Ten, including Illinois, New York, and Pennsylvania, have no PPT. The remaining five levy a PPT but allow specific exemptions (e.g., for manufacturing equipment).

DISCUSSION

Opponents of the PPT argue that it is a major reason that the cost to locate or expand a business in Michigan is higher than in competing states. Many surveys reveal that business leaders see the tax as one of the top five anti-competitive provisions of Michigan law. Some analysts argue that since the nontax costs of production sometimes are higher in Michigan than elsewhere (labor costs usually are mentioned), to attract new jobs the tax burden for business actually should be *lower* than in competing states.

Opponents also argue that administrating the PPT is burdensome and unfair. Unlike the tax on real property, personal property is self-reported by firms. Each year, every business must provide the local assessor with a form itemizing each piece of personal property and its age. The assessor then assigns a value, using depreciation schedules published by the state, to each item. This self-reporting of taxable property, opponents argue, is time-consuming for businesses and leads to substantial underreporting.

Some analysts point out, however, that eliminating, reducing, or reforming the personal property tax is easier said than done, and they point to several difficulties.

- Reducing or eliminating the tax would affect the revenue stream to all types of Michigan governments: city, county, township, school, and state.
- Since the PPT base varies widely across the state, the effect of reducing or eliminating the tax would be much greater in some places than in others.
- The tax is, in large part, a *local* tax that would be changed or eliminated by *state* law. This fact usually leads to discussion about state reimbursement to locals for lost revenue, but short of a constitutional amendment, it is not possible to *guarantee* such in future years.
- It is very difficult to quantify the economic effect of reducing the PPT. Opponents and proponents of changing or eliminating the tax agree that taxes negatively affect economic development, but they disagree on how *much* and *when*. Opponents of changing the PPT do not believe that a reduction/elimination will lead to economic activity increases sufficient to offset the direct revenue loss.
- There also is a long list of technical questions involved in reform. For example, personal property never has been tightly defined in state law. Although some categories of personal property

are mentioned in statute, in general, personal property simply is defined as *all property that is not "real."* Since in Michigan the tax rates on real and personal property always have been identical, this vagueness has not been too troublesome. But the statutory distinction between the two will become very important if personal property comes to be taxed at a lower rate than real property.

Current Reform Proposals

There are many proposals to reduce or eliminate the personal property tax in Michigan. Some have been introduced as legislation, some offered informally by policymakers and interested parties.

10/10 Plan

Each year an increasing proportion of personal property would be exempt from taxation, starting at 10 percent and increasing by 10 percent every year, until the tax is eliminated in year ten. Such a phaseout could be adjusted to fit any proportion or time frame.

Reverse New Jersey Plan

This too gradually would reduce the personal property tax, but the phaseout would be based on the property's age. For example, in year one, property ten years or older could be exempt; in year two, property nine years and older; and so on. Although the tax would continue, it ultimately would apply only to personal property in the year in which it is purchased.

New Jersey Plan

The personal property tax gradually would be phased out by exempting all *newly acquired* property. Ultimately, as existing property is scrapped, the tax would be repealed entirely.

Tax Threshold

Because of the perceived administrative burden of the PPT, some call for keeping it but allowing an exemption for property of value below a certain threshold. For example, all property valued at less than $10,000 could be exempt.

Replacement Revenue

The personal property tax would be eliminated immediately and the revenue replaced or partially replaced by increasing another tax, for example, the single business tax.

Local Option

Each local government could exempt from tax all or a portion of personal property within its jurisdiction; the revenue lost would not be replaced by the state.

Revised Depreciation Schedules

Finally, many analysts and policymakers argue that the tax's administration should be improved. The state publishes the depreciation schedules that local assessors use to calculate tax liability. Based on the property's age and useful life, these schedules determine depreciation factors that then are multiplied by the property's original cost; this calculation establishes the item's taxable value. The depreciation schedules have not undergone major revision since 1964—more than 30 years. Furthermore, many observers argue that the state's use of only a few schedules results in the actual value of personal property being misrepresented for many business. The state has hired outside consultants to review the current depreciation schedules; recommendations for change may be presented in early 1999. While schedule revisions probably will lead to an overall reduction in tax collections, some individual companies could see a tax increase.

See also Business Taxes; Economic Development: State Financial Incentives.

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