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Headlee Amendment and Tax Issues: What Your Library Needs to Know

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Taxing 101

- We will discuss the following issues that affect the total taxes levied by or on behalf of a library:
  - Review some basic terms and tax concepts.
  - The Headlee Amendment.
  - Proposal A.
  - Truth in Taxation.

Taxing 101

- There are three types of value placed on taxable property:
  - True Cash Value – how much is the property worth, i.e., the usual selling price (not necessarily the sales price).
  - State Equalized Value – the local assessor's determination of the property's value. SEV is one-half of the True Cash Value.
  - Taxable Value – the tax base is the SEV subject to a rate of inflation cap on any increase in value.

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Taxing 101

- Example of calculating the tax bill for a property using the three values:
  - Property is purchased for $200,000. The True Cash Value is determined to be $200,000 in this example.
  - The assessor determines that the SEV is $100,000 (one half the TCV).
  - Since the property has just been purchased, the TV is set at the same level as the SEV of $100,000 (this taxable value will vary from the SEV as the years go by after the sale…as described later).
  - The district library levies 1.0 mill for library purposes.
  - 1.0 mill equals $1.00 for every $1,000 of taxable value ($.001).
  - So, the property owner will pay $100.00 for library service on this property.
  - The formula is the millage rate x taxable value = tax due

    ($.001 x 100,000) = $100.00

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Taxing 101

- Example of calculating the tax bill for the capped tax formula:
  - TV is the prior taxable value – same owner $100,000.
  - TV for 2017 is $100,000 x 2017 rate of inflation (1.009) = $100,900.
  - TCV increases to $250,000; SEV increases to $125,000.
  - But, TV is now $24,1000 less.

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Taxing 101

- The "tax base" in a jurisdiction is the total taxable value of property within that jurisdiction.
- The county equalization director is responsible for identifying the tax base in any taxing jurisdiction. The taxable value is sent to and approved by the State Tax Commission.
- Total millage revenue is based on the *taxable value of the property (tax base)* x <u>the millage rate</u>.
- So, the following laws impact the total tax rate and taxable value of property – both factors in this equation.

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What is the Headlee Amendment?

- Voters approved the Headlee Amendments in 1978.
- These are amendments to the Michigan Constitution of 1963, specifically the amendments were to Article IX, Sections 24 - 34.
- This session will focus on the part of the Headlee Amendments that most effect libraries. (Section 31.)

What is the Headlee Amendment?

- Did you know?
  - The “Headlee Amendment” is named after its proponent, Richard Headlee.
  - Mr. Headlee worked for Taxpayers United for Tax Limitation at the time the amendment was passed. This was a private organization.
  - He ran for Governor in 1982 but was not successful in that campaign.

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What is the Headlee Amendment?

- The Headlee Amendments were essentially to place constitutional tax limitations on automatic increases to the millage rate without a vote. For libraries, the main impact is:
  - The need to have an election.
  - The limit on the amount of taxes.

Voter Approval Needed

- Section 25.

Property taxes and other local taxes and state taxation and spending ***may not be increased above the limitations specified herein without direct voter approval***. The state is prohibited from requiring any new or expanded activities by local governments without full state financing, from reducing the proportion of state spending in the form of aid to local governments, or from shifting the tax burden to local government. A provision for emergency conditions is established and the repayment of voter approved bonded indebtedness is guaranteed. Implementation of this Section is specified in Sections 26 through 34, inclusive, of this Article.

Voter Approval Needed

- Section 31.

Units of Local Government are hereby prohibited ***from levying any tax not authorized by law or charter when this Section is ratified or from increasing the rate of an existing tax above that rate authorized by law or charter when this Section is ratified***, ***without the approval of a majority of the qualified electors of that unit of Local Government voting thereon***. If the definition of the base of an existing tax is broadened, the maximum authorized rate of taxation on the new base in each unit of Local Government *shall be reduced to yield the same estimated gross revenue as on the prior base*. If the assessed valuation of property as finally equalized, excluding the value of new construction and improvements, increases by a larger percentage than the increase in the General Price Level from the previous year, the maximum authorized rate applied thereto in each unit of Local Government shall be reduced to yield the same gross revenue from existing property, adjusted for changes in the General Price Level, as could have been collected at the existing authorized rate on the prior assessed value.

The limitations of this Section shall not apply to taxes imposed for the payment of principal and interest on bonds or other evidence of indebtedness or for the payment of assessments on contract obligations in anticipation of which bonds are issued which were authorized prior to the effective date of this amendment.

Voter Approval Needed

- So, there is no new tax or tax increase without voter approval.
- This requirement does not apply if the law permitting a tax without voter approval was in effect before the 1978 amendment.
- The statutes governing libraries contain an example of this.

Voter Approval Needed

- Section 1 of PA 164 states as follows:

  The city council of each incorporated city may establish and maintain a public library and reading room for the use and benefit of the inhabitants of the city. ***The city council may levy a tax of not to exceed 1 mill on the dollar annually on all the taxable property in the city.*** *If approved by a majority of the voters voting on the proposal at the regular annual election, the city council may increase the tax levied by not to exceed 1 additional mill on the dollar annually on all the taxable property in the city.* The tax shall be levied and collected in the same manner as other general taxes of the city, and shall be deposited in a fund to be known as the "library fund."

- The Headlee Amendment did not take away the ability of a City Council to levy this millage for a Section 1 City library.

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Headlee Rollbacks

- The State Tax Commission describes the Headlee Reduction Fraction as follows:

  > "The Headlee millage reduction fraction intends that, ignoring additions and losses, any current <u>operating millage</u> must be reduced if it would produce more tax dollars, adjusted for inflation, than it did last year." (Emphasis added.)

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Headlee Rollbacks

- So, basically increased tax rates can only include those that are increased due to inflation (and additions such as new construction).
- The local taxing unit cannot collect a millage based on any increases greater than that amount, even if property values are rising or transfers (sales) increase.
- This is accomplished through the application of Headlee Rollbacks to the millage rate.

Headlee Rollbacks

- What are losses?
  - Destroyed property
  - Exempt property (including personal property tax exemptions)
  - Property decrease in occupancy
- What are additions?
  - Omitted property
  - New construction
  - Previously exempt property
  - Replacement construction

Headlee Rollbacks

- What is not included as an addition or a loss?
  - Uncapping
  - Rising home values
- Also, the amount of losses and additions will be included in taxable value in the next year.

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Headlee Rollbacks

- How is the reduction factor determined?

$$\frac{(\text{prior year's taxable value} - \text{losses}) \times \text{inflation rate multiplier}}{\text{Current year's taxable value} - \text{additions}}$$

$$\text{2016 MRF} = \frac{(\text{2015 taxable value} - \text{losses}) \times 1.003}{\text{2016 taxable value} - \text{additions}}$$

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Headlee Rollbacks

- How is the reduction factor determined using a taxable value for 2015 ($1 million) and 2016 ($1.3 million) with a 2% inflation rate for 2016 (no additions or losses for simplicity)?

$$\frac{(\$1{,}000{,}000 - \$0) \times 1.02 = \$1{,}020{,}000}{1{,}300{,}000 - \$0}$$

2016 MRF = .7846

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Headlee Rollbacks

- What is the new millage rate?
  - In 2015, with $1,000,000 in taxable value, the 1.0 mill raised $10,000.
  - If the Rollback had not occurred, the library would have raised $13,000 in 2016 due to the increased taxable value, for a $3,000 (23%) gain.
  - Applying the millage reduction factor of .7846 mill, the $1,300,000, the millage would now generate $10,200.
  - The is the same as the 2015 taxable revenue plus the 2% rate of inflation.

Headlee Rollbacks

- So, the purpose is to limit the amount of taxes to the rate of inflation that that a taxing unit can levy to essentially eliminate huge gains in taxable value.
- A Rollback would be applied so that the revenue collected would be adjusted for inflation.

What is a Headlee Override?

- The recent decrease in property values has demonstrated how the Headlee has affected local units of government.
- As property values decreased, Headlee Rollbacks did not occur. Even if the millage rate remained static, the dropping property values meant that the municipality was raising less money.
- As the recession ends, the millage rates start to roll back again.

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What is a Headlee Override?

- Now that property values are on the rise, the limits of the Headlee amendment are generally back in effect.
- As a result, the local units cannot recover the losses they suffered over the last several years.
- As a result, communities are considering “Headlee Overrides.”

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Headlee Override -Ballot Language

- A “Headlee Override” is a request by voters to reset the millage rate back to the original amount.
- This “Headlee Rollback” amount would be considered a “new additional” tax and must be approved by voters.
- In the General Property Tax Act, a ballot proposal must contain a clear statement indicating whether the proposed millage is a renewal of a previously authorized millage or the authorization of a new additional millage.
- So how do voters ask for to reset the millage?

Headlee Override -Ballot Language

- **Example**: The voters in the New Township District Library district authorized a millage of 1 mill 10 years ago and the millage is in perpetuity. However, it has been reduced to .87 mill due to Headlee Rollbacks and the Library does not have enough revenue to meet the needs of the community. The Library wants to levy 1.0 mill again.
- To restore the full mill, the Library must ask voters to approve an additional "new millage" of .13 mill. This is traditionally called a Headlee Override because you are only asking voters to allow the Library to levy the original amount.

Headlee Override -Ballot Language

- **<u>Example</u>**: The voters in the New Township District Library district authorized a millage of 2.0 mills 20 years ago and the millage is expiring this year. The millage rate has been reduced to 1.80 mills. The Library does not have enough revenue to meet the needs of the community and they want to be able to levy 2.0 mills again.
- How do we draft the ballot language?

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Headlee Override - Ballot Language

- The General Property Tax Act requires, among other things, that a ballot proposal contain a clear statement indicating whether the proposed millage is a renewal of a previously authorized millage or the authorization of a new additional millage.
- Renewal:
  - Must be a true renewal of the millage as last levied.
  - Using the example, if the voters authorized a millage of 2.0 mills years ago, but it has been reduced to 1.80 mills, the "renewal" must only be a "renewal" of 1.80 mills.
  - To restore the full mill, the voters must also ask for an additional "new millage" of .20 mill.

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Headlee Override – Ballot Language

- **Example**: The voters in the New Township District Library district authorized a millage of 2.0 mills 20 years ago and the millage is expiring this year. The millage rate has been reduced to 1.45 mills. The Library does not have enough revenue to meet the needs of the community and they want to be able to levy 2.0 mills again.
- With this example, there is an added issue.

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Headlee Override -- Ballot Language

- Do we need one or two questions?

- MCL 211.24f provides that "[a] taxing unit that levies millage under this act shall not submit a single question to the electors of the taxing unit requesting both the renewal of voter authorized millage and the authorization of new additional millage if the new additional millage is greater than .5 mill."

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Headlee Override -- Ballot Language

- Do we need one or two questions?
  - Answer: Two questions are needed because the public body must ask for a renewal of 1.45 mills and additional new millage of .55 mill to recover the amount reduced by Headlee. The new millage exceeds .5 mill, so two questions are required if the Library wants to ask for the 1.45 mills as a "renewal."
  - Other options.

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A Headlee "Head's Up"

- District Libraries must pay attention to the Rollbacks of municipalities in the district.
- By law, millage rates must be uniform in any taxing jurisdiction.
- By way of example, if a District Library is comprised of Municipality A and Municipality B, the Library must levy the same rate uniformly in a district.

A Headlee "Head's Up"

- If the municipality is added to the district, the new municipality must also pay the same rate.
- For example, District Library originally approved a 20 year millage five years ago, the original authorization is for 1.0 mill. The millage rate has not been rolled back to .9 mill and levied uniformly in both municipalities.
- If a new municipality joins, the District Library must not levy an amount exceeding .9 mill in the new district even thought the ballot proposal will identify the 1.0 mill initial authorization.

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Proposal A

- Proposal A was also a constitutional amendment.
- It was designed to address high property taxes and how schools were funded.
- Growth on the taxable value of property is limited to:
  - Rate of inflation; or
  - Five (5%) percent, whichever is less.

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Proposal A

- Proposal A allowed for "uncapping." "Uncapping" occurs when the property is sold or transferred.
- The taxable value is reset to the State Equalized value, which is one half of the true cash value.
- However, the limits of Proposal A go into effect again after the uncapping.

Proposal A and Headlee

- So how do Headlee and Proposal A work together to lower taxes?
  - Headlee lowers the tax rate (millage rate) that a property owner pays.
  - Proposal A restricts the increase in taxable value of an individual property.
  - Since the tax rate is the *millage rate x the taxable value*, restricting growth on both components of taxation lowers taxes and provides less revenue for taxing jurisdictions.

Fact

- Did you Know: Property Tax is the single largest tax in Michigan.
- $13B in 2014 compared to:
  - $8.7B Individual Income Tax;
  - $8.3B Sales and Use Tax;
  - $3.5B Transaction Taxes;
  - $1B Corporate Income Tax.

Truth in Taxation

- Truth in Taxation is another aspect of property taxation that affects local tax revenue.
- If the library desires to levy a millage rate for operating purposes in excess of the Base Tax Rate ("BTR"), the library must comply with Section 24e of the General Property Tax Act. MCL 211.24e.

Truth in Taxation

- Put another way, a local unit of government must approve any levy that produces more tax dollars that last year’s actual levy.
- This must ignore additions, losses and building and site fund millages.

Truth in Taxation

- How is the Base Tax Rate determined?

2016 BTR = 2015 operating levy rate x 2016 BTRF

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Truth in Taxation

- How is the Base Tax Rate Fraction determined?

$$\frac{\text{(prior year's taxable value – losses)}}{\text{(Current year's taxable value based on SEV – additions)}}$$

2016

$$\text{BTRF} = \frac{\text{(2015 taxable value – losses)}}{\text{(2016 taxable value – additions)}}$$

- Must use the same amounts for additions and losses as used for the Headlee Rollback.

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Truth in Taxation

- How is the Base Tax Rate Fraction determined?

$$\frac{(1{,}000{,}000)}{(1{,}300{,}000)}$$

<u>2016</u>

<u>BTRF =.7692</u>

- Must must use the same amounts for additions and losses as used for the Headlee Rollback.

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Truth in Taxation

- Using the "Headlee" example, the Headlee Rollback rate would be .7846 mill

2016 BTR = 2015 BTR x BTRF

.7692 mill = 1.0 mill x .7692 BTRF

- Now, we see the Truth in Taxation rate is .7692 because Truth in Taxation does not account for inflation.
- Illustration: In 2015, $1,000,000 raises $10,000. In 2016, the taxable value increased to $1,300,000 so 1 mill would raise $13,000. Applying the Truth in Taxation millage rate of .7692 mill, the $1,300,000 in taxable value now raises $10,000 as it did the previous year.

Truth in Taxation

- The municipality may not levy a millage rate greater than the Truth in Taxation rate if that rate is lower than the Headlee Rollback rate without a vote of the taxing jurisdiction.
- But, the municipality may only levy up to the Headlee Rollback rate.
- In this example, .0154 mill is the difference (.7847 Headlee Rollback millage - .7692 Truth in Taxation millage).

Truth in Taxation

- There are two ways to comply with the Truth in Taxation hearing. This requires notice, a public hearing and a resolution of the board).
  - A separate Truth in Taxation hearing
  - Or, if the taxing body complies with Section 16 of the Uniform Budget and Accounting Act during the budget process.

Truth in Taxation

- For either way, the public notice must include a statement that "the property millage rate proposed to be levied to support the proposed budget will be a subject of this hearing." (In 11 point, boldface type!)

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Truth in Taxation v Headlee

- Taxing Jurisdictions are prohibited by law from imposing a tax greater than permitted by a Headlee Rollback, *without voter approval*.
- Taxing jurisdictions may impose a tax rate greater than the Truth in Taxation levels (but not greater than the Headlee Rollback rate), but only if the legislative body holds a hearing and improves the increased rate.

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Questions

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