



City of Ann Arbor Income Tax Feasibility Frequently Asked Questions

Municipalities in Michigan are statutorily required to provide certain services such as police, fire, district court, etc. These services are funded through a variety of revenue sources. The two most significant revenue sources are operating millage (property tax) and state revenue sharing. The Michigan economy has resulted in declining property values, thereby reducing property tax revenues. Lower state sales tax collections are also reducing state shared revenue.

During the past several years, the City of Ann Arbor has made significant reductions in costs, including a 25-percent reduction in the number of employees, without a substantial reduction in services. Despite these cost reduction efforts, the revenue available to the city is declining at a rate which will impact critical services in the near future.

The City of Ann Arbor is a vibrant and engaging community that has been recognized as a top destination to live and work. The University of Michigan plays a central role in the vibrancy of Ann Arbor as do the many parks and recreation activities. Unfortunately, Ann Arbor parks, the University of Michigan plus other tax-exempt organizations comprise 40 percent of the total real-property ownership in the city, leaving the remaining 60 percent to pay for most general-fund city services.

An income tax could potentially help to diversify and stabilize the city's revenue stream, and shift some of the tax burden from property owners and residents to non-residents. City Council requested an update to a 2004 income tax study to help identify solutions to the city's shrinking tax revenue situation. The full report and Frequently Asked Questions (FAQs) are available on the City's website at www.a2gov.org.

Below are key points for voters to consider regarding a potential Ann Arbor City income tax.

- Under PA 284 of 1964, local voters must approve a local income tax and the tax is limited to 1 percent on residents and corporations and 0.5 percent on non-residents.
- If an income tax is authorized, City Council would also have to establish an exemption level which taxpayers can use to reduce their taxable income. Other Michigan communities utilize between \$600 and \$3,000 per eligible exemption.

- Ann Arbor's City Charter requires that the adoption of an income tax must be accompanied by a repeal of the city's largest millage – its Operating millage. A resident with qualifying homestead property would see a 14-percent reduction in his or her property taxes. [Since the city only receives a portion of the total property taxes collected, the city would see a 37 percent reduction in revenue from property taxes.]
- Administration of an income tax is estimated to cost approximately \$3 million annually.
- Initial estimates suggest the city could recognize an additional \$8 to 14 million annually, net of administrative fees, by adopting an (1% resident / 0.5% non-resident) income tax depending on which exemption level is established.
- Adoption of an income tax would require the drafting of ballot language, approval of the language by the Michigan Attorney General, and a vote of Ann Arbor residents to amend the City Charter.
- Local income taxes are deductible on federal tax returns if you itemize, and a portion of income tax paid to Michigan cities is deductible from Michigan state income tax.
- There are 22 other Michigan communities who utilize a local income tax.

Frequently Asked Questions:

1. Why should residents *consider* approving an income tax?

Answer: Michigan's property tax laws limit revenues to municipalities. These limits have been in place for decades and have already created budget shortfalls. Now, lower property values and declining state revenue sharing are jeopardizing basic services provided by many communities. The following are a few reasons why Ann Arbor residents should consider approving an income tax:

- The city is in a very difficult financial situation. Reductions in important city services are planned to be implemented in 2010 and 2011 in order to balance the budget.
- Two of the many things which contribute to Ann Arbor being a desirable place to live and work are the University of Michigan and the city's extensive park system. Both of these properties are tax exempt and are the largest contributors to the fact that 40 percent of the property in Ann Arbor is tax exempt.
- As a consequence of state tax limitations, the millage for property tax may not be increased without the vote of the people.
- State law does not permit cities to institute other types of taxes such as a sales tax or an entertainment tax (eg.: ticket tax on sporting events).
- An income tax, which supplements a lower property tax, would rebalance the tax burden from just property owners and residents to include the non-resident workforce.
- City Council commissioned a feasibility study of the potential effects of instituting a city income tax in lieu of an operating tax millage. This study was completed and indicates a new income tax could raise from \$8 to \$14 million in additional revenue.

- The city has 75,000 non-resident commuters who utilize some city services but do not pay local taxes.
 - The many organizations that are exempt from paying property taxes would, through their employees, begin to pay a portion of the costs of city services.
2. Would property taxes be eliminated if an income tax is approved?
 Answer: Only the General Operating millage is eliminated. All remaining millages, including voter approved millages for land acquisition (green belt & parks), street resurfacing, and Parks would not be affected. Although the city collects property taxes for other jurisdictions like the schools, library, county, and the state, it keeps approximately 28 percent of the monies collected. The other taxing jurisdictions would not see any reduction in property tax revenues. A resident with a homestead exemption would see approximately 14-percent reduction in property taxes while the city would incur a 37-percent reduction in property tax revenues.
 3. Will I pay more in total taxes (property tax plus income tax)?
 Answer: It varies depending on individual circumstances. Appendix C of the Income Tax Feasibility study includes examples of how individuals may be impacted. These examples include a resident who owns and lives in their home, a resident who rents, a resident who qualifies for a senior or disabled exemption, and a non-resident who commutes to work in Ann Arbor.
 4. How would a residential rental property owner be affected?
 Answer: The property owner would see a reduction in property taxes. The rental resident would incur an income tax of 1 percent. It's uncertain to what extent market pricing pressures will or will not drive landlords to pass the property tax reduction on to renters.
 5. How will I as a senior citizen who lives on a fixed income be affected?
 Answer: Senior citizens and the disabled would receive an extra income tax exemption. If a person in this category owns their home, they will see a reduction in their property taxes and an increase in income taxes, but only after deducting a personal exemption and the extra exemption. (If a \$1,000 exemption level were approved, a senior or disabled person would be able to deduct \$2,000 from taxable income before applying the 1 percent tax rate.)
 6. If an income tax is approved, how would it be collected?
 Answer: Companies would start withholding income taxes from individuals' paychecks and/or quarterly payments could be made. A local income tax form would be required to be filed by April 15. If approved by voters, the earliest an income tax would take effect would be January 2011.
 7. How much will an income tax raise?
 Answer: If an income tax is approved by the voters, the City Council would also need to establish the exemption (or deduction) level. The amount of additional revenue raised would depend upon whatever exemption level is approved. The feasibility report prepared by Plante Moran has several scenarios which could be considered ranging from \$7.6 million to \$14.2 million.
 8. What did the income tax study find and where can I read the report in its entirety?
 Answer: The full report is available on the city's website at www.a2gov.org.

9. What services would the additional revenue from an income tax support?
 Answer: The proceeds of an income tax, which would not be available until July 2011, would support the same activities the general operating levy supports. Most of these activities are in the City's General Fund where significant service reductions are contemplated in July 2010. City Council is responsible for how tax revenues are spent, but the following is a list of imminent issues which need to be addressed:

- Reductions in Fire Services (equiv. to 14 fire fighters) \$1.4 mil.
- Lower State Shared revenue 2.0 mil.
- Lower non-tax related revenues 1.1 mil.
- Possible DDA reimbursement if income tax passes 0.8 mil.
- Under compliance during startup of income tax ??? mil.
- Increase in cost of doing business in 2012 ??? mil.

10. What's the average taxable income for Ann Arbor residents and what is the average taxable value of residential property?

Answer: The average taxable value of residential property in Ann Arbor is \$110,000. The taxable income for residents is not available but the following household income is available from the 2000 U.S. Census:

HOUSEHOLDS BY INCOME

Level of Income			Number of Households	Percent
Less than		\$10,000	4,724	10%
\$10,000	to	\$14,999	2,543	6%
\$15,000	to	\$24,999	5,221	11%
\$25,000	to	\$34,999	4,894	11%
\$35,000	to	\$49,999	6,873	15%
\$50,000	to	\$74,999	8,046	18%
\$75,000	to	\$99,999	5,024	11%
\$100,000	to	\$149,999	5,129	11%
\$150,000	to	\$199,999	1,594	3%
\$200,000	or more		1,696	4%
Total			45,744	100%

Median Income \$46,299

11. Instead of an income tax, how much would a Headlee override provide in additional property tax revenue if the general operating millage was increased to its original maximum in the City Charter of 7.500 mils?

Answer: If the General Operating levy was increased to the maximum established in the City Charter, it would provide approximately \$6 million in additional revenue.

12. If the income tax isn't passed what city services will be impacted?

Answer: If an income tax isn't passed or another alternative approved, the 2011 fiscal year plan outlines significant cuts that would be implemented in July 2010. These cuts include the reduction of 14 full-time firefighters, the closing of the senior center and Mack pool among other reductions.