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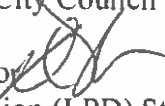
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TO: The Honorable Detroit City Council

FROM: David Whitaker, Director 
Legislative Policy Division (LPD) Staff

DATE: February 25, 2018

RE: **Income Tax Reporting Regarding Non-Detroit Residents
Earning Income in the City**

President Pro Tem Sheffield directed the Legislative Policy Division (LPD) to consult with the Office of the Chief Financial Officer (OCFO) and draft an ordinance that mandates periodic reporting to the City by employers of non-Detroit residents who earn income in the City, which is therefore taxable by the City at the rate of 1.2%. Due to the City's well-documented fiscal challenges, the importance of collecting every single potential revenue dollar cannot be overstated. And because of state laws limited mandatory withholding and other factors, it has been widely alleged that many nonresident workers who actually earn income by work performed in the City may nevertheless not be paying local income tax on those earnings. Therefore this is a problem that cries out for solutions to benefit the City and our residents.

At the outset, it should be noted that after multiple discussions with OCFO and Pro Tem Sheffield and her staff regarding this assignment, there are apparently non-resident employees working in Detroit who may be of concern: e.g., employees of City contractors vs. employees (or other agents or partners) of innovative, "new economy" business models (designed in part to avoid tax liabilities that would otherwise apply, as part of their business model), such as Uber and Arbnb.

LPD notes that: 1) no single legislative strategy would even provide for, much less implement and enforce, income (or property or business) tax liability of all potential categories of workers under this broad "non-resident employer (or principal)" umbrella; 2) OCFO has stated that they believe, through their powers to conduct audits and request discovery and investigation of information from any corporations conducting business in the City, they already have the powers they need to pursue

the efforts to collect all the revenue the City is owed under law¹; and 3) It would take \$25 million worth of untaxed income by non-resident employees who fit any category subject to local income tax, at the low rate of 1.2%, to generate new tax collected revenue of \$300,000; an extremely high target income figure for what may in reality be available, generating at best modest tax receipts.

The importance of the issue of increasing income tax revenues to the City even led to recent action in the State legislature to increase income tax collections in the City, via House Bills 4618 and 5025 (attached). This lame duck session legislation from December 2018 amended the City Income Tax Act and the Revenue Act to provide new income tax collection procedures for the City. Employers outside Detroit are authorized to voluntarily register to withhold taxes of their employees who are residents of Detroit. Hopefully this new State legislation will lead to significant increased income tax revenue, and additional local legislation addressing the issue of nonresident employees who earn taxable income in the City.

After duly consulting with OCFO, LPD offers the following draft language in response to this assignment:

“All entities who are parties to any contract with the City of Detroit, for delivery of goods or services of any kind, shall file an annual report by no later than January 31 of each year, identifying all employees, officials, subcontractors and other agents of the contractor who earned income within the previous calendar year performing work within the City of Detroit, as well as the amount of such income earned by each and every such individual performing work within the City of Detroit during the previous calendar year.”

The January 31 date is chosen primarily so that the reports would be received by Council in a timely fashion for consideration during the budget process over the next few months. It is LPD’s understanding that revenue collection officials within OCFO would then cross-check the data provided by such reports against income tax returns either filed, or not, by the named individuals, to determine whether or not the City is owed additional tax revenue by those individuals. Although ProTem’s original referral requested quarterly reporting, OCFO advises that they do not have the personnel to conduct such reviews on a quarterly basis, so Council may wish to consider adjusting the required reporting periods to annually.

If Council has any other questions or concerns regarding this subject, LPD will be happy to provide further research and analysis upon request.

¹ Of course, having those powers and effectively using them – particularly against entities actively trying to avoid liability – may well be two different things, but the effectiveness of OCFO’s audit, investigation, discovery and enforcement procedures is beyond the scope of this report.

Legislative Analysis



CITY INCOME TAX COLLECTION PROCEDURES

Phone: (517) 373-8080
<http://www.house.mi.gov/hfa>

House Bill 4618 as enacted
Public Act 456 of 2018

Analysis available at
<http://www.legislature.mi.gov>

House Bill 5025 as enacted
Public Act 553 of 2018

Sponsor: Rep. Wendell Byrd
House Committee: Tax Policy
Senate Committee: Government Operations
Complete to 2-11-19

SUMMARY:

House Bills 4618 and 5025 modify the City Income Tax Act and the Revenue Act, respectively, to provide new city income tax collection procedures for the City of Detroit ("City") and the Michigan Department of Treasury ("department"). Pursuant to an agreement signed under the City Income Tax Act, the department provides administration, enforcement, and collection functions for the City's city income tax.

House Bill 4618 authorizes an employer outside a city with a population of 600,000 or more that imposes a city income tax (i.e., the City of Detroit) to voluntarily register to withhold taxes of employees that are residents of the City. An employee of the employer who elects to withhold city income taxes for the City cannot opt out. An employer who elects to withhold city income taxes for the City must withhold city income taxes from all employees who are residents of the City.

If an employer elects to withhold taxes and subsequently wants to discontinue the practice, the employer must file a written notice with the City and the department as acting administrator of the city income tax for the City.

The bill authorizes the City to recover city income taxes with interest and penalties without a judgment or order from a court through the imposition of a lien on property owned or wages, or other income, reported on a Federal W-2 or 1099 form. The lien attaches to the property for seven years after the date of attachment and may be extended for another seven years by refile within six months of the initial lien's expiration.

The lien takes precedence over all other liens and encumbrances, except bona fide liens recorded before the date a lien filed under this bill is recorded. Bona fide liens only take precedence to the extent of disbursements made under a financing arrangement before the 46th day after the date of the tax lien recording or before the person making the disbursements had actual knowledge of a tax lien recording under this ordinance, whichever is earlier.

A purchaser or succeeding purchaser of property upon which a lien executed under this bill is attached is personally liable for the unpaid taxes due. The liability is limited to the value of the

property less any proceeds that were applied to the balances due on secured interests which are superior to the lien recorded.

The bill also permits the City to cause a demand to be made on a taxpayer for payment of city income taxes due. The demand applies to property owned and wages, or other income, reported on a Federal W-2 or 1099. If the liability is not paid within ten days of the demand and if proceedings are not taken to review the liability, a warrant may be issued. The City may levy the amount of the deficiency on all property and sell the property found within the State for the payment of the amount due, the cost of executing the warrant, and the additional penalties and interest.

A person who refuses or fails to surrender any property subject to levy, upon demand by the City, is personally liable to the City for a sum equal to the value of the property not surrendered, not to exceed the amount due for which the levy was made together with the costs and interests on the sum. Additionally, a person failing to surrender property without reasonable cause is liable for a penalty equal to 50% of the value of the property not surrendered plus costs and interest.

Upon satisfaction of the tax liability, the City must file a release of the lien within 20 business days of payment. If the City files for a lien and, upon request, determines that the taxpayer named on the lien has no interest in certain properties owned by another person, the City must file a certificate of nonattachment with all due haste but not more than five days after the City determines that the lien was recorded or filed against property to which the City does not have a lien interest.

Once the City determines that a tax liability is satisfied, it must serve a release of levy on the person that was served a warrant or warrant-notice of levy not more than ten days following the payment of the tax liability. Additionally, if, after issuing a warrant or warrant-notice of levy, the City determines that the property is not subject to levy, the City must serve a release of levy with all due haste but not more than five business days after the determination.

The City must reimburse a person for any fee paid as a result of an erroneous recording or filing of a lien or erroneous issuance and service of a warrant or warrant-notice.

If the tax liability is satisfied and the City subsequently files a lien, warrant, or warrant-notice of levy determined to be in error, the City must file for recording a certificate of withdrawal of the lien, in the case of a lien, or issue a release of levy, in the case of the warrant or warrant notice of levy, with all due haste but not more than five business days after the determination of error is made.

House Bill 5025 adds "a known city income tax liability for a [city income] tax administered by the department" to the list of liabilities to which the department may apply a state income tax refund. Currently, the City of Detroit is the only city that has an agreement with the department to administer and collect city income taxes on its behalf.

MCL 141.506, et al. (House Bill 4618)
MCL 205.30a (House Bill 5025)

BRIEF BACKGROUND:

The City Income Tax Act (1964 PA 284) permits a city to levy an income tax after the city has adopted the uniform city income tax ordinance. Cities can only impose an income tax if one of the following applies: 1) the city had a city income tax prior to 1995, or 2) after 1995, the city income tax is approved by the voters of the city. The Department of Treasury website provides links for city income tax forms for 22 Michigan cities.¹

Treasury began processing Detroit's individual income taxes in January 2016 (for tax year 2015) and corporate income taxes in January 2017 (for tax year 2016). According to a Treasury press release, the transition was part of Detroit's post-bankruptcy management plan.² The city income tax rates are: 2.4% (resident), 1.2% (non-resident), and 2.0% (corporate). In 2017, the Detroit city income tax totaled \$292.7 million of which \$151.1 million came from non-residents. Of the total amount collected between \$10.0 and \$15.0 million is received from corporations.

FISCAL IMPACT:

The bills would increase city income tax revenues for the City of Detroit by an unknown, but likely significant amount. While administrative costs for the City of Detroit and the Department of Treasury could increase, any costs would be more than offset by the increase in revenue due to the enhanced collection methods.

If additional cities signed agreements with the Department of Treasury, the provisions in House Bill 5025 would apply and would presumably lead to increased city income tax revenue collections for those cities by an unknown amount.

Fiscal Analyst: Ben Gielczyk

■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.

¹ Michigan Department of Treasury, "City Income Tax Forms": <http://www.michigan.gov/taxes/0,4676,7-238-44143-287984--,00.html>

² State of Michigan, Department of Treasury, "State to begin processing Detroit individual income tax returns; changes to take effect for 2015 tax year": http://www.michigan.gov/documents/taxes/CITA_Press_Release_505696_7.pdf

Act No. 553
Public Acts of 2018
Approved by the Governor
December 27, 2018
Filed with the Secretary of State
December 28, 2018
EFFECTIVE DATE: December 28, 2018

**STATE OF MICHIGAN
99TH LEGISLATURE
REGULAR SESSION OF 2018**

Introduced by Rep. Byrd

ENROLLED HOUSE BILL No. 5025

AN ACT to amend 1941 PA 122, entitled "An act to establish the revenue collection duties of the department of treasury; to prescribe its powers and duties as the revenue collection agency of this state; to prescribe certain powers and duties of the state treasurer; to establish the collection duties of certain other state departments for money or accounts owed to this state; to regulate the importation, stamping, and disposition of certain tobacco products; to provide for the transfer of powers and duties now vested in certain other state boards, commissions, departments, and offices; to prescribe certain duties of and require certain reports from the department of treasury; to provide procedures for the payment, administration, audit, assessment, levy of interests or penalties on, and appeals of taxes and tax liability; to prescribe its powers and duties if an agreement to act as agent for a city to administer, collect, and enforce the city income tax act on behalf of a city is entered into with any city; to provide an appropriation; to abolish the state board of tax administration; to prescribe penalties and provide remedies; and to declare the effect of this act," by amending section 30a (MCL 205.30a), as amended by 1995 PA 116.

The People of the State of Michigan enact:

Sec. 30a. (1) If a taxpayer claims a refund that the department determines is valid as provided in section 30(2), and the department identifies a liability of the taxpayer described in subsection (2), the department shall first apply the amount of the refund as provided in subsections (2) and (3), and the excess, if any, shall be refunded or credited as provided in section 30.

(2) The amount of a refund described in subsection (1) shall be applied to the following in the order of priority stated:

(a) Any other known tax liability of the taxpayer to this state.

(b) Any other known liability of the taxpayer to this state, including a liability to pay support if the right to receive the support has been assigned to the state and the liability is the basis of a request for tax refund offset from the office of child support.

(c) Any of the following in the order of priority received, unless otherwise provided by law:

(i) A support liability of the taxpayer that is the basis of a request for tax refund offset from the office of child support, other than as provided by subdivision (b).

(ii) A writ of garnishment or other valid court order issued by a court of competent jurisdiction and directed to this state or the state treasurer to satisfy a liability of the taxpayer.

(iii) A known city income tax liability for a tax administered by the department through an agreement entered into under section 9 of chapter 1 of the city income tax act, 1964 PA 284, MCL 141.509.

(iv) A levy of the internal revenue service to satisfy a liability of the taxpayer.

(v) A liability to repay benefits obtained under the Michigan employment security act, 1936 (Ex Sess) PA 1, MCL 421.1 to 421.75, to which the taxpayer was not entitled, upon a request for tax refund offset from the Michigan unemployment insurance agency.

(3) If the claim for refund is reflected on a joint tax return, the department shall allocate to each joint taxpayer his or her share of the refund. The amount allocated to each taxpayer shall be applied to his or her respective liabilities in the order of priority stated in subsection (2).

(4) If the department determines that all or a portion of a refund claimed on a joint tax return is subject to application to a liability of an obligated spouse, the department shall notify the joint taxpayers by first class mail sent to the address shown on the joint return. The notice shall be accompanied by a nonobligated spouse allocation form. The notice shall state all of the following:

(a) That all or a portion of the refund claimed by the joint taxpayers is subject to interception to satisfy a liability or liabilities of 1 or both spouses.

(b) The nature of the other liability or liabilities and the name of the obligated spouse or spouses.

(c) That a nonobligated spouse may claim his or her share of the refund by filing a nonobligated spouse allocation form with the department of treasury not more than 30 days after the date the notice was mailed.

(d) A statement of the penalties under subsection (7).

(5) A nonobligated spouse who wishes to claim his or her share of a tax refund shall file with the department a nonobligated spouse allocation form. The nonobligated spouse allocation form shall be in a form specified by the department and shall require the spouses to state the amount of income or other tax base and all adjustments to the income or other tax base, including all subtractions, additions, deductions, credits, and exemptions, stated on their joint income tax return or other joint tax return that is the basis for the claimed refund, and an allocation of those amounts between the obligated and nonobligated spouse. In allocating these amounts, all of the following apply:

(a) A federal deduction for 2-income married persons shall be allocated to the spouse with the lower income who claims the deduction.

(b) Individual income shall be allocated to the spouse who earned the income. Joint income shall be allocated equally between the spouses. The tax base appropriate to tax other than income tax shall be similarly allocated.

(c) Each spouse shall be allocated the personal exemptions he or she would be entitled to claim if separate federal returns had been filed, except that dependency exemptions shall be prorated according to the relative income of the spouses.

(d) Adjustments resulting from a business shall be allocated to the spouse who claimed income from the business.

(e) A homestead property tax credit shall be allocated to the spouse who owned the title or held the leasehold interest in the property claimed as a homestead. A homestead property tax credit for property jointly owned or leased shall be allocated jointly between the spouses.

(f) Ownership of other assets relevant to the allocation shall be disclosed upon request of the department.

(6) A nonobligated spouse allocation form shall be signed by both joint taxpayers. However, the form may be submitted without the signature of the obligated spouse if his or her signature cannot be obtained. The nonobligated spouse shall certify that he or she has made a good faith effort to obtain the signature and shall state the reason that the signature was not obtained.

(7) A person who knowingly makes a false statement on a nonobligated spouse allocation form shall be subject to a penalty of \$25.00 or 25% of the excessive claim for his or her share of the refund, whichever is greater, and other penalties as provided in this act.

(8) A nonobligated spouse to whom the department has sent a notice under subsection (4), who fails to file a nonobligated spouse allocation form within 30 days after the date the notice was mailed, shall be barred from commencing any action against this state or the state treasurer to recover an amount withheld to satisfy a liability of the obligated spouse to which a joint tax refund is applied under this section. The payment by this state of any amount applied to a liability of a taxpayer under this section shall release this state and the state treasurer from all liability to the obligated spouse, the nonobligated spouse, and any other person having or claiming any interest in the amount paid.

(9) The department shall promulgate rules under the administrative procedures act of 1969, 1969 PA 306, MCL 24.201 to 24.328, as necessary to implement this section. The rules shall include a procedure for assuring that a taxpayer subject to application of a refund under this section and section 30 has received or will receive notice and an opportunity for a hearing with respect to the liability to which the refund is to be applied.

(10) As used in this section:

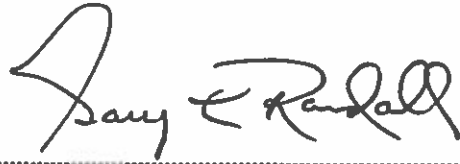
(a) "Nonobligated spouse" means a person who has filed a joint income tax return or other joint state tax return and who is not liable for an obligation of his or her spouse described in subsection (2).

(b) "Obligated spouse" means a person who has filed a joint income tax return or other joint state tax return and who is liable for an obligation described in subsection (2) for which his or her spouse is not liable.

(c) "Office of child support" means the agency created in section 2 of the office of child support act, 1971 PA 174, MCL 400.232.

Enacting section 1. This amendatory act does not take effect unless House Bill No. 4618 of the 99th Legislature is enacted into law.

This act is ordered to take immediate effect.



.....
Clerk of the House of Representatives



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Secretary of the Senate

Approved

.....
Governor