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Wisconsin Municipalities Depend Most on Property Taxes Among Midwest States

WPF Report Finds Local Governments Here Have Fewer Revenue Options Than Neighbors

MILWAUKEE AND MADISON – Cities and villages in Wisconsin rely more heavily on property taxes than any other state in the Midwest, and to a greater degree than most states nationally, according to a new report by the nonpartisan, independent Wisconsin Policy Forum.

In 2015, Wisconsin municipalities received 42.2% of their revenues from the property tax, but only 1.6% from sales and income taxes combined, WPF noted. Nationally, on average, municipalities got 23.3% of their revenues from the property tax with an additional 21.3% from sales and income taxes.

The increased dependence on the property tax is the result, in part, of state aid failing to keep pace with inflation, according to the report. From 1975 to 1997, state aid provided a larger share of municipal revenues here than property taxes. Since then, the situation has reversed, with property taxes in 2015 accounting for more than twice as much of local revenue as state aids.

At the same time, the state has also imposed limits on how much municipalities may raise property taxes annually to support their operations; those limits have been set generally at 0% except for increases in property values due to new construction. In the decade before these limits took effect, municipal property taxes rose an average of 5.7% annually, but in the following decade the average increase fell to 3.4% annually.

The report notes Wisconsin's property tax limits appear to be the most restrictive among states that also depend heavily on this tax. Four of the 10 most property tax-dependent states have no such limits on increases, while the other five include allow for increases that would typically be greater than those permitted here.

The report, "Dollars and Sense: Is it time for a new municipal financing framework in Wisconsin?" examines trends in municipal finance, compares Wisconsin's municipal funding structures to other Midwest states and the nation, and provides insights on alternative financing options.

Other states tend to rely on a broader combination of revenues, including local sales taxes, local income or license taxes, charges for services, and federal aids. In Wisconsin, state law allows only the state to levy an income tax and reserves the sales tax for the state, counties, and a limited number of municipalities that qualify as "premier resort areas."

Among the 12 Midwest states (Wisconsin, Illinois, Iowa, Indiana, Minnesota, Michigan, Kansas, Nebraska, North Dakota, South Dakota, Missouri, and Ohio), the report notes that:

- Only two states (Illinois and North Dakota) rely more heavily on state aid and less on charges to fund municipalities;
- Wisconsin is the only state in which municipalities generally are authorized to levy only the property tax. In all other states in the region, some municipalities can levy at least one other broad tax;
- Wisconsin is the only state in the region in which property taxes represent the largest share of municipal revenue. In seven states, charges for services are the primary revenue source.
- Wisconsin has the lowest combined state and local sales tax rate in the region, with an average of 5.44%. The combined rate in Michigan, the next-lowest state, is 6%, while the rate is still higher in Kansas at 8.68%.

The report does not recommend any specific course of action, but lays out several options for policymakers, and weighs the advantages and disadvantages of each. The options include:

- Doing nothing and maintaining the status quo. The report suggests that without increases in state aids, municipalities would grow more reliant on the property tax and, in some cases, might tap the only other available options to them, including raising local vehicle registration fees ("wheel taxes"), going to referendum to exceed property tax limits, or relying more heavily on borrowing.
- Increasing the use of fees. The report suggests this would be the "least challenging" of the proposed changes, but it could mean the costs would fall more heavily on lower-income residents than those with higher incomes.
- Allowing local option sales taxes. The report suggests this would allow municipal revenues to grow along with economic expansion and capture funds from visitors and commuters, but the sales tax is considered regressive and its use in only some communities could create "tax islands." Approval of such taxes could be made contingent on voter approval. However, sales may be more volatile than property taxes and might raise taxes overall.
- Increasing the state sales tax. The report suggests the additional funds generated from the tax could be targeted to municipalities or distributed according to existing state aids programs. However, the report notes, "given … the proposal's greater breadth, it might prove even less popular than a local options sales tax."
- Allowing local income taxes. The report suggests this option would fall more heavily on upper-income residents than lower incomes, would grow with the economy, and provide greater balance to municipal revenues, but it would be the most subject to economic volatility and be more complicated to implement than other options.

The report concludes that "Wisconsin voters and their leaders will need time to decide whether and how to approve an alternative revenue framework for cities and villages. Still the urgency of doing so is real. Signs of stress are appearing and, with unemployment low and revenues on the rise, the state is better placed to address these issues than any time since 2000."

The research was commissioned by the League of Wisconsin Municipalities, Wisconsin Association of REALTORS, and the Greater Milwaukee Committee. The complete report can be found here.