



EVALUATING A LOCAL-OPTION SALES TAX POLICY FOR DETROIT

In a Nutshell

- Michigan's local governments rely primarily on property taxes to fund general public services. The largest cities and counties continue to struggle to sustain and grow local revenues to meet their residents' needs. The heavy reliance on only property taxes, which are subject to multiple limitations on growth, makes revenue generation difficult for areas with weak tax bases, such as in the city of Detroit.
- While the path to adopting a local sales tax option for Michigan's local governments is daunting, having access to taxes that diversify local revenues would help improve the fiscal health of the state's most populated cities and counties, allowing them to benefit from the increased retail and commerce activity. Authorizing a local sales tax in Michigan will require amending the state Constitution, adopting state statutes authorizing local sales and use taxes, the local governing body to enact an ordinance, and voter approval of a new tax.
- Estimating the revenue potential of a one percent local sales and use tax in Detroit is challenging. Data on sales tax collections is not available by geographic location, does not accurately jive with state sales and use tax laws, nor is household spending data and expenditures on taxable purchases available for city visitors. The Research Council estimates potential revenues for a one percent sales tax in Detroit to yield about \$72 million annually.

Michigan's local governments, especially its major cities and larger counties, continue to struggle to sustain and grow local revenues to fund a range of public services. Michigan affords local governments few options to levy local taxes. The issues stem from heavy reliance on property taxes, with multiple limitations on growth, and for cities like Detroit, weak tax bases that make revenue generation difficult. Except for a few special taxes and a city income tax, most local governments rely heavily on property taxes and state revenue sharing.

The City of Detroit is reviewing potential local option taxes to raise city revenues to improve city services and address needs it anticipates in the future. Rising out of bankruptcy, the city is working to put city services on par with surrounding communities, supplement pension payments that are again a city responsibility after a 10-year hiatus, capture economic benefits from growth in visitor activity downtown, and potentially also provide tax relief.

Cities and counties, with larger geographical footprints such as the City of Detroit, are the units most likely to benefit from a local sales tax, given the tax revenues will be higher in areas with greater retail, business, and visitor activity.

Local Taxes Currently Levied in Detroit

Michigan cities primarily rely on property taxes and state-shared revenue to fund general services. City residents, visitors, tourists, and businesses pay taxes to jurisdictions other than the city, including the state, county, school districts, special regional districts, and others. In the City of Detroit, several county taxes are imposed on lodging, auto rentals, and the state imposes excise taxes imposed on liquor, tobacco, and marihuana.

Because of the layering of all these taxes, many of which are levied at the highest (or among the highest) rates in the state, Detroit residents are among the highest taxed in the state. Some of the taxes, such as the non-resident income tax and casino taxes, export the tax burden to outsiders, but city residents bear a heavy burden.

Background on Sales and Use Taxes

Revenues from sales and use taxes, second only to income taxes, help fund government operations and services, at both the state and local levels. All but four states authorize sales taxes at either the state or local level: Delaware, New Hampshire, Montana, and Oregon.¹ Alaska does not levy a state sales tax, but its local governments may levy local sales taxes. Across the country, the sales and use taxes provided 32 percent of state tax collections, and 13 percent of local collections in 2025.^{2,3} States determine how to allocate sales tax revenues through their appropriations process. Some portion of the revenues may be designated for specific purposes, such as school aid or revenues sharing, as is required by law in Michigan.

Currently, 37 states allow at least some of their local governments to levy a local-option, retail sales tax. How local sales taxes are structured differs across the states: variation exists in which local units are allowed to levy taxes, how many local units actually do levy taxes, and how broad a local tax's base is. Some states allow different types of local units to levy local-option sales tax, which can lead to overlapping local sales tax rates in some areas. Almost all of the local-option sales taxes across the states are administered at the state level.

Michigan's sales tax is imposed on the retailer for the privilege of making sales at retail. The use tax is imposed on the privilege of using, storing, and consuming certain tangible personal property, plus telephone, telegraph, and other leased wire communication services; used auto sales between individuals; and the use of transient hotel and motel rooms.

Michigan's six percent sales tax rate, which does not include any local sales taxes, ranks 38th in the country. Seventeen states levied a combined state and local sales tax rate of seven percent or greater in 2025.

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Local-Option Tax Issues to Consider

The lack of alignment of local revenue sources with the local economy is a challenge for Michigan's current local government revenue structure. Communities lack taxes that capture the business activity taking place within their boundaries. While the local property tax revenues reflect growth in property values, they do not produce revenue gains from increased business activity from bustling downtowns and job growth.

When levied at the most local level of government (i.e., city, village, township level) local taxes can create administrative difficulties and local competition, introduce economic distortions by creating incentives for people to live or work or purchase items in jurisdictions with lower taxes, and intensify socioeconomic disparities across local units of government. Some of these concerns over economic distortions, socioeconomic disparities, and local competition can be addressed by authorizing local-option taxes for larger cities, counties, or regions.

Access to a variety of local-option taxes may allow a particular government to tailor the taxes it levies on activities that reflect its economic strengths (e.g., retail or tourism). On the other hand, some local taxes could diminish a region's economic competitiveness, make it more vulnerable to economic downturns, and limit the state's ability to raise rates on state taxes.

Perspectives on Sales and Use Taxes

In theory, well-designed sales and use taxes have several components.

- The tax base should be broad and include both tangible goods and services.
- The taxes should be imposed on the product or service in the state or local government where it is consumed.
- The taxes should provide a sustainable and reliable source of revenue to support ongoing public services.
- The taxes should be simple to understand by taxpayers as well as consumers.

Regressivity. Tax economists agree that the sales tax is generally regressive, imposing a greater economic burden on lower-income households than on higher-income households

Tax Avoidance and Tax Exportation. What often appeals to local policymakers is that local sales taxes are 'exported' or paid by visitors to the geographic area through spending on activities such as dining and entertainment. However, when a significant portion of consumers try to avoid higher taxes when tax rates vary between areas, or through online retailers, retailer retention, local employment, and general economic activity can be affected.

Sales Tax Competition and Neutrality. A local-option sales tax not only impact individual consumer habits, but also potentially affects the decisions of retailers to relocate elsewhere to neighboring communities or states. Due to consumers' and businesses' sensitivity to tax differences, neutrality is a key

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concept to consider. A tax should not alter, or should minimally alter, business decisions over where to locate, what to produce, or whom to employ.

Evolving Tax Base. Since states' initial adoption of sales taxes, the economy has changed from one based on manufacturing and production of goods to a more service-based economy. With the increase in professional and personal services offered consumers are buying fewer tangible goods. Many goods previously in the form of a physical product, such as a movie, software disc, or video game, are now delivered in a digital format and are not taxed.

The tax base is also affected by exemptions. A most recent example is the exemption of sales tax on motor fuel that was adopted as part of Michigan's 2025 Transportation Funding Package.⁴

Balance in Overall Mix of Local Revenues. Balance in the overall mix of taxes as revenue sources for a local government is achieved when the overall tax burden is spread over several different tax bases. Property, income, and sales should all contribute to the financing of government. A tax structure that is out of balance risks creating economic disincentives that could cause people and businesses to locate elsewhere or to conduct business elsewhere and can place the governmental unit at risk if one tax suffers an economic decline.

Michigan's State Sales and Use Taxes

Michigan retailers are required to submit the sales and use taxes collected on their sales to the Department of Treasury. The tax is applied to the gross proceeds of a transaction for use or consumption. The total sales tax rate is limited to six percent in the Michigan Constitution.⁵ (The use tax rate is also six percent, but is statutorily set.) Exemptions are allowed for purchases made by certain purchasers, such as not-for-profit organizations or the federal government. In addition, the sale of certain items is exempt from tax. The most notable exemptions include the sale of food not for immediate consumption or groceries, prescription medications, water, and sales to religious and other not-for-profit organizations.⁶

A final, but important, characteristic of Michigan's sales tax is that very few services are taxed. Originally adopted when the economy had fewer professional and personal services, the tax base has not kept up with shifts in commerce activity. Plus, the adoption of various tax exemptions has eroded the original tax base.

Benefits of a Local-Option Sales Tax

Michigan law authorizes some local-option taxes, but local governments continue to rely heavily on local property taxes. Cities may levy a local income tax, but only 24 Michigan cities currently do. The inability to levy sales taxes leaves local governments without a full complement of tax options from which to choose to create a stable revenue stream.

Local governments gain several advantages with the ability to levy a local option sales tax.

- The availability of a local sales tax increases revenue diversity for Michigan governments.
- Revenue diversification of the tax mix could benefit local governments by allowing local governments to benefit directly when retail and economic activity grows in their communities. However, the opposite could occur if such activity declines.
- A local tax would lessen dependence on the state to share its tax revenues. Although the state shares state sales tax revenue, the total level of state revenue sharing payments can be unpredictable.
- A supplementary revenue source could provide local governments the resources to offer their residents general tax relief, especially in the state's counties and larger cities, and capture economic activity from visitors and tourists from outside the area who frequent lodging, restaurants, and entertainment in the community.

Legal Authority for Sales Taxes and Local Taxation in Michigan

Michigan's counties, cities, villages, and townships derive their authority to levy taxes through both the 1963 Michigan Constitution and state statutes. These laws stipulate the type of taxes that may be levied, the maximum tax rates and the items included or exempted from the tax bases. They also specify which types of local governments are authorized to levy certain types of taxes.

The legal authority to levy Michigan sales and use taxes, either at the state or the local level, spans across several constitutional provisions and state statutes. While some of the legal provisions are quite specific, others contain some ambiguity. For instance, it does not state whether the sales tax rate limit applies to only state sales taxes or if the limit applies to combined state AND local sales taxes. under the existing language of the state Constitution as that authority remains legally untested.⁷ Additionally, while the Constitution provides for sharing a percentage of sales tax revenues collected with local governments, it does not specify whether the sharing provisions would apply to any local sales tax revenues.

Legal Path to Authorizing and Adopting a Local Sales Tax in Michigan

Pursuing authorization requires careful attention to the legal process for obtaining constitutional approval, state legislative approval, local legislative approval, and finally, securing local voter approval.

Amending the Michigan Constitution. Consistent with the 1970 Attorney General opinion, providing room to increase the state sales tax rate, clarifying how local tax revenues would apply to existing constitutional earmarks, and clarifying whether local government could levy a local sale tax would entail an amendment to the 1963 Constitution.

State Legislative Authorization. Article VII, Sections 2 and 21, attempted to grant home rule charters more self-governance powers, including taxing authority, than general law units.⁸ However, despite the constitutional authority granted to home rule counties, cities, and villages, local governments could not levy taxes other than property taxes after 1964 due to Public Act 243 of 1964.

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Michigan's existing local-option tax laws are drafted as uniform laws that define the tax base, administrative responsibilities, the disposition of revenues, and the permissible tax rates.

Local Legislative Approval. Once a state law is in place to permit a local government to levy a local sales tax, the local government's legislative body must also adopt an ordinance.

Local Voter Approval. The local government will also have to place the question of a new tax before voters for approval, pursuant to Article IX, Section 31, of the 1963 Constitution.

Ecommerce Sales and the Streamlined Sales Tax Agreement

Tax administration – collection, enforcement, and auditing of tax filings – is another important consideration for those considering enacting a local sales tax. Complying with the 2018 the landmark U.S. Supreme Court decision in *South Dakota v. Wayfair, Inc.* (138 S. Ct. 2080 (2018)) will be an important consideration.⁹ As a member of the Streamlined Sales Tax Agreement (SSUTA), a collaborative effort of state governments, and the business community,¹⁰ Michigan has made remitting sales and use taxes simpler for ecommerce and remote businesses.

The following are the most important SSUTA provisions that apply to all states party to the agreement.

- State level administration and collection of state and local sales and use taxes.
- Uniformity in the state and local sales tax bases.
- Uniformity of major sales tax base definitions.
- Central, electronic registration system for all member states.
- Simplification of state and local sales tax rates.

Should Michigan pursue a uniform local sales tax option for cities or counties, the administration requirements for local sales taxes under the SSUTA will have to be met for the state to continue to be a member of the SSTA. Not participating in the SSTA would bring significant administrative and collection challenges, and potentially a loss of sales tax revenue to the state. Michigan state sales tax collections from out-of-state retail sales rose from \$12.9 million in 2015 to \$158.3 million in 2024.¹¹

Designing Uniform Local Sales and Use Taxes

Tax Bases. Given that retaining membership in the Streamlined Sales Tax Agreement (SSUTA) is in Michigan's best interest, the state and local sales tax bases must be the same. Although this is a tax design component that improves simplicity and administration of the tax, it will preclude local governments from providing specific exemptions they may want through the sales and use taxes, unless those exemptions are adopted for both state and local taxes.

Administration. To mitigate the burden of sales tax collections for out-of-state

sellers and avoid challenges to the U.S. Commerce Clause, SSUTA requires local sales taxes to be collected at the state level. There is administrative efficiency for state-level collection but local governments most likely would have to include an administrative fee for collection services as they budget revenues from a new tax.

Disposition of Revenues. Local policymakers may wish to select some specific purposes that appeal to local residents to gain more support for additional local taxation. In Detroit, these purposes could include funding for its post-bankruptcy pension debts, street maintenance, increases in public safety personnel, or property tax relief.

Potential Revenues. Estimating revenues a Michigan local government could collect by levying local sales and use taxes is recognized by tax analysts as notoriously difficult. Not only is accurate data of what amount-of-purchases-are-made-where unavailable due to Michigan's sales tax collection system, but the complexity of the sales and use tax bases does not lend themselves to the way consumer or business spending information is collected by public data collecting agencies.

With a local sales tax rate higher in nearby jurisdictions, consumers will more easily be able to shop across borders. The Research Council was unable to model cross-border shopping to identify use taxes that would be owed. Moreover, exported taxes to suburbanites and tourists are also difficult to estimate and can vary from year to year depending on events and the economy.

The total revenues the City of Detroit may collect with a one percent local sales tax were calculated by based on retail spending as a percentage of the sales and use tax spending base. Under this approach, it is estimated that a one percent local sales tax may raise nearly \$72 million annually.

Alternatives to a Local Sales Tax Option

A local sales tax option gives local governments the opportunity to diversify their revenues stream. However, given the challenging legal pathway to authorizing local governments to levy local sales taxes, it may be helpful to review alternative paths, and evaluate their feasibility as well.

Raising the Statewide Sales Tax Rate Will Increase Amounts Available for Revenue Sharing. With a statewide sales tax increase, not only will constitutional revenue sharing payments rise for cities, villages, and townships across the state, the state would also gain additional sales tax revenues. For example, in the City of Detroit, if the total state sales tax rate were seven percent, the City of Detroit would receive just under \$60 million in addition to its current constitutional revenue sharing allocation. Note, an increase to the sales tax rate will still require an amendment to the state constitution.

Reforming and Broadening the Sales Tax and Use Tax Base May Mitigate the Need to Raise the Rate. Since Michigan adopted its sales tax in 1933, the general economy has evolved from one based on the purchases of tangible goods to one which includes the delivery of digital products, and more services, both professional and personal. In addition, many exemptions have been adopted,

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further eroding the tax base. By broadening the base to recognize modern retail activity and revising exemptions, it may be possible to capture new revenues to share with local governments and potentially avoid a significant rate increase. Amendments to the sales tax base and capturing new revenues would require state law changes.

Adding Amusement Activities and Ticket Sales to State Sales and Use Taxes Could Bring Revenues to Cities with Entertainment Venues. The state could amend the state sales tax law to subject admission tickets to the state sales tax. This change may also bring additional revenues to other Michigan cities that host events and entertainment centers if there is geographic distribution of revenues raised from this addition.¹² The state legislature would have to amend and adopt changes to the Sales and Use Tax Acts.

Adopting a New Local Excise Tax Could Generate Special Purpose Revenues. A local excise tax instead of a local general sales tax is another option to increasing local revenues. The authorization path for the adoption and approval of a local excise tax will require state and local legislative approval and a local vote.

Choosing Not to Pursue a New Local Tax Option Could Be an Opportunity for Municipal Finance Reform. Completing a review of the state's municipal finance system could address some of the structural fiscal challenges faced by Michigan's local governments. Embarking on an evaluation and reform of the state's municipal finance structure is a demanding endeavor that will take state support, proactive leadership, and dedication from all levels of government to be successful.

Conclusion

As Michigan's local governments, especially its largest cities and counties, seek to diversify their revenue sources and take advantage of growing local economies, a local sales tax option may be a good fit. The legal path to authorizing a local sales tax is a formidable task, however, and no city, even Detroit, should make the effort without widespread support.

Some alternatives to establishing a local sales tax option could also be used to increase local revenues. They include increasing the statewide sales tax rate and capturing additional constitutional revenue sharing, modernizing the state sales tax base, and evaluating existing exemptions, including on amusements and entertainment tickets, and the taxability of digital products and services, or choosing an entirely different revenue enhancement policy.

The ability to estimate how much a one percent local sales tax in Detroit is quite difficult, given the lack of data on household spending and visitor activity that jives with the state's sales and use tax laws. Policymakers should consider a revenue range of approximately \$42.3 million to \$71.2 million annually from a one percent local sales tax.

Endnotes

- 1 Investopedia, <https://www.investopedia.com/terms/s/salestax.asp>
- 2 The Tax Foundation, <https://taxfoundation.org/data/all/state/sales-tax-rates/>
- 3 Investopedia, <https://www.investopedia.com/terms/s/salestax.asp#toc-use-taxes>
- 4 Citizens Research Council of Michigan, *Assessment of the 2025 Transportation Funding Package*, Report 423, https://crcmich.org/PUBLICAT/2020s/2025/rpt423-assessment_of_2025_transportation_funding_package.pdf
- 5 Taxes on residential use of electricity, gas, and heating fuels are limited to 4 percent
- 6 Citizens Research Council of Michigan, *Outline of the Michigan Tax System*, updated November 2025, <https://crcmich.org/publications/outline-of-the-michigan-tax-system-39th>
- 7 Citizens Research Council of Michigan, *Issues Relative to the Constitutionality of Local Sales Taxation in Michigan*, Report 305, 1992, https://crcmich.org/publications/constitutionality_local_sales_tax-1992
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- 9 *South Dakota v. Wayfair, Inc*, https://scholar.google.com/scholar_case?case=12308977437779741578&hl=en&as_sdt=6&as_vis=1&oi=scholarr
- 10 The Streamlined Sales Tax Governing Board, Inc., <https://www.streamlinedsalestax.org/>
- 11 See particularly Sections 301,302, and 308 of the agreement
- 12 Citizens Research Council of Michigan, *Evaluating Local Option Admission Taxes in Michigan Cities*, <https://crcmich.org/publications/evaluating-local-option-admission-taxes-in-michigan-cities>

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