



Perspectives on
Michigan's State
Personal Income Tax

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Citizens Research Council

- Founded in 1916
- Statewide
- Non-partisan
- Private not-for-profit
- Promotes sound policy for state and local governments through factual research – accurate, independent and objective
- Relies on charitable contributions from Michigan foundations, businesses, and individuals
- *www.crcmich.org*

Eric Lupher, President of Citizens Research Council of Michigan



- 30 years with Citizens Research Council
- Expert on Michigan local government, including
 - intergovernmental cooperation
 - governance issues
 - municipal finance
- Also has researched such issues as
 - state taxes
 - state revenue sharing
 - highway funding
 - unemployment insurance
 - economic development incentives
 - stadium funding

Jordon Newton, Research Associate for Citizens Research Council of Michigan



- Citizens Research Council's new researcher focused on state affairs
- Recent graduate of the Michigan State University Master of Public Policy Program
- B.A. in Economics from Gonzaga University

Perspectives on Michigan's State Personal Income Tax

Eric Lupher, President, and Jordon Newton, Research Associate

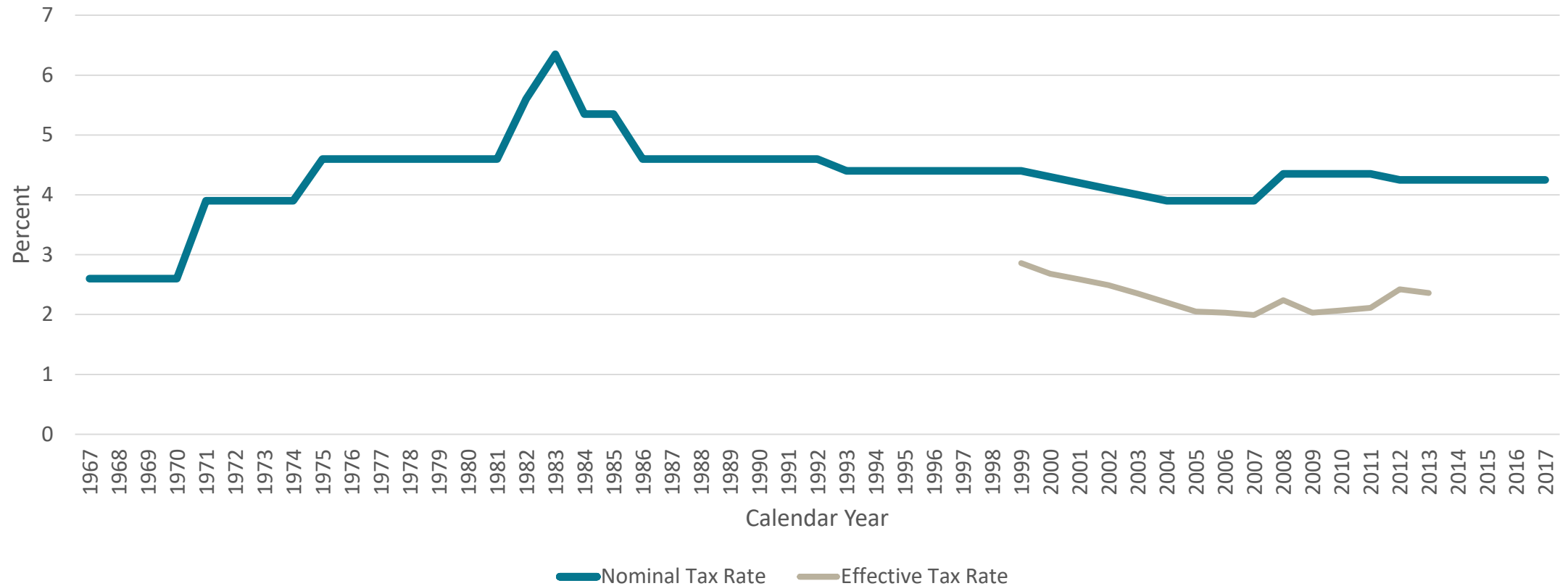
Citizens Research Council of Michigan Webinar
May 9, 2017

Plan for Today's Presentation

1. A look backward – previous tax cut efforts
2. Putting current tax revenues into historic perspective
3. Perspective on Michigan's tax competitiveness
4. The role of the personal income tax in funding state government
5. Perspectives on an income tax cut

Lessons of History

Michigan's Individual Income Tax Rate History



Source: Effective Tax Rate from *Michigan's Individual Income Tax 2013*, Office of Revenue and Tax Analysis in Michigan Department of Treasury, May 2016

Past Income Tax Rate Rollback Efforts

- State – 0.1 percentage point from 4.4% in 1999 to 3.9% in 2004
 - Contributed to structural budget deficit and worsened Michigan's Single State Recession
- Detroit – 1998 PA 500 reduced City Income Tax resident tax rate 0.1 percentage point/ 0.05 percentage points for nonresidents until new rates became 2% for residents/1% for nonresidents
 - Process halted if certain unfavorable financial conditions occur.
The conditions for suspending the rate reductions are any three of the following:
 1. two consecutive years of withdrawals from the city's budget stabilization fund or exhaustion of the fund balance;
 2. a year-to-year decline in income tax revenue, after adjusting for inflation, of more than 5%;
 3. a city unemployment rate of 10% or higher; or
 4. a provision which compares the growth ratio of the city's taxable value with the comparable statewide figure and computes a ratio which must fall below .80 (in order for the ratio to fall below 0.80 with the state taxable value holding constant, the city's taxable value would have to decline 20%).

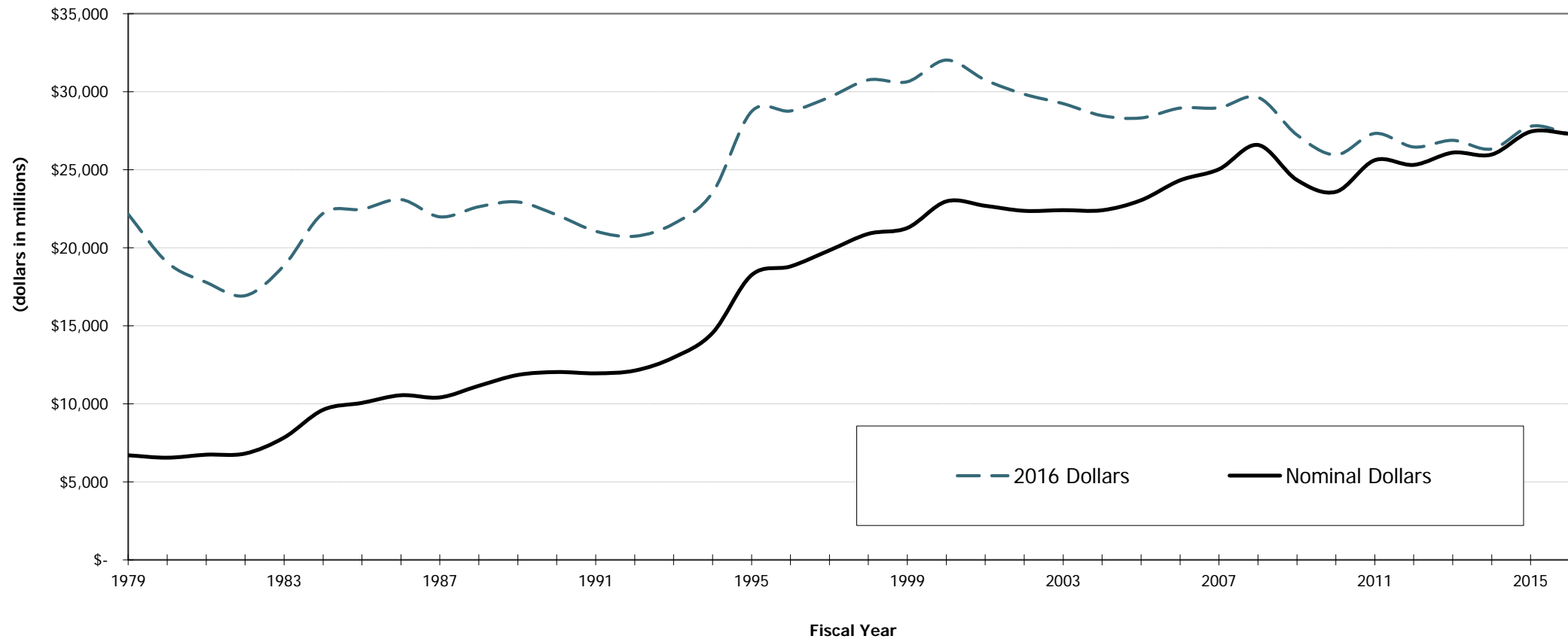
PA 180 of 2015

- After 2023 reduces rate by growth in excess of inflation if the increase from one year to the next in total General Fund/General Purpose revenue exceeded 1.425 times inflation for the same period
 - Allows for rate reductions, not increases
 - Reductions come out of GF/GP budget
 - Keeps SAF harmless

Three methods of measuring adequacy of overall tax structure and income tax specifically

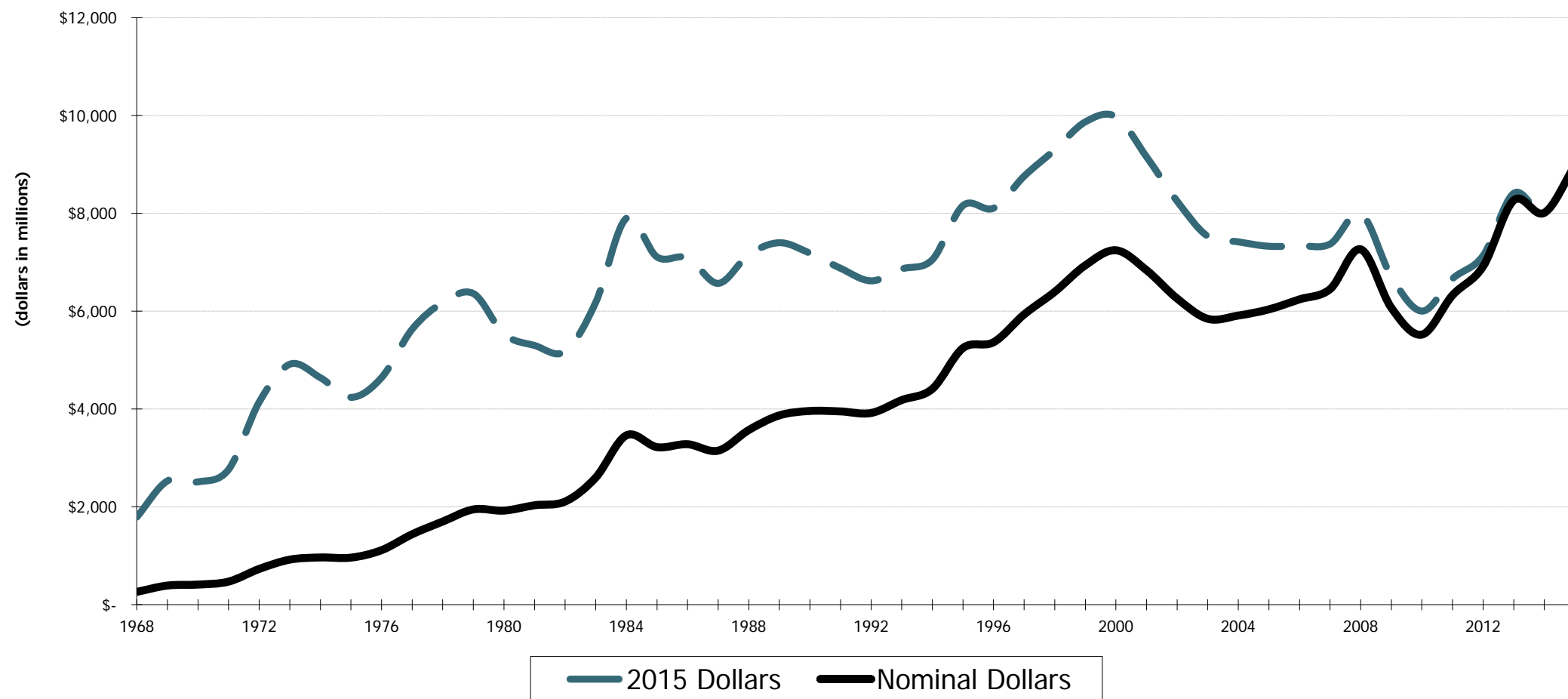
1. Against itself over time
2. Against constitutional revenue limit
3. Against other states

State Tax Revenues, 1979-2016



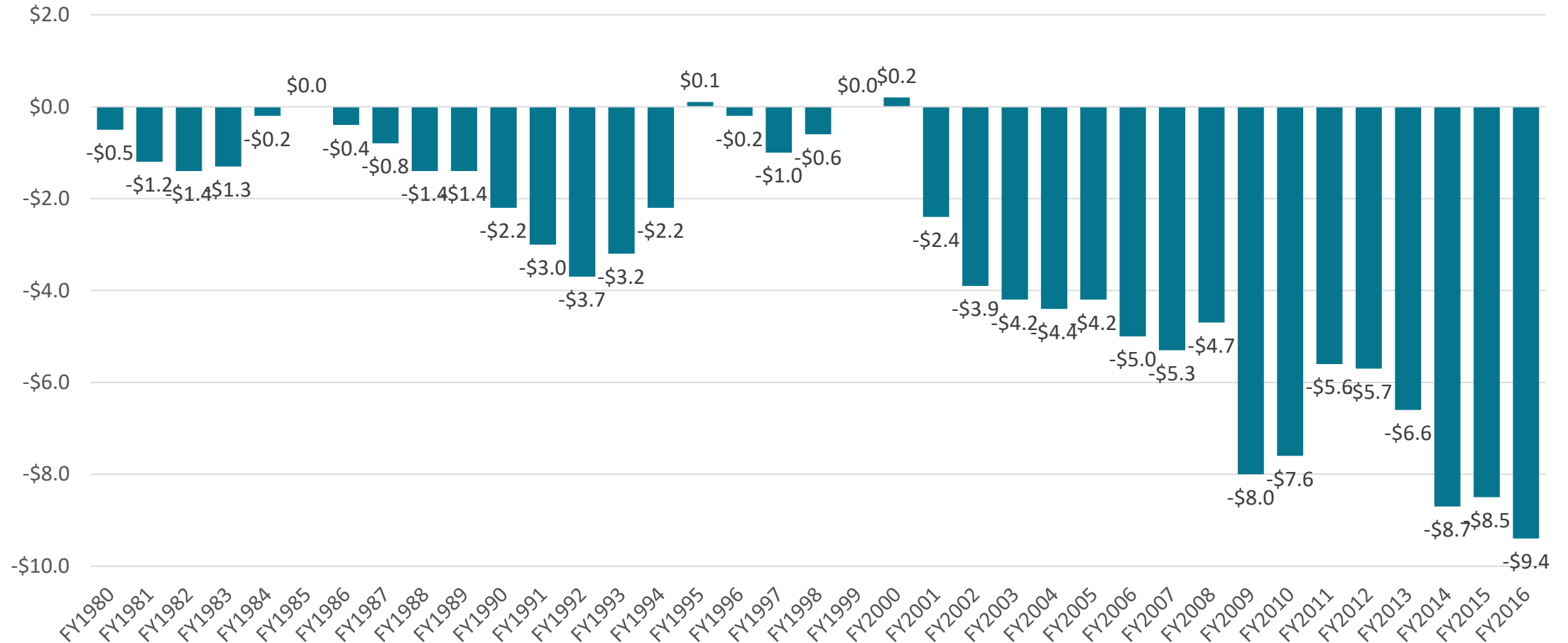
Michigan Individual Income Tax Revenues, 1968-2015

(Nominal and Real)



Constitutional Revenue Limit

(Statutory implementation of Art. IX, Section 26 of Michigan Constitution (Headlee) limits state revenue to 9.49% of personal income)



Source: House Fiscal Agency, State Budget Overview, January 2015, www.house.mi.gov/hfa/archives/pdf/state_budget_overview_jan2015.pdf

Michigan's Tax Competitiveness

Is Michigan a “High Tax” State?

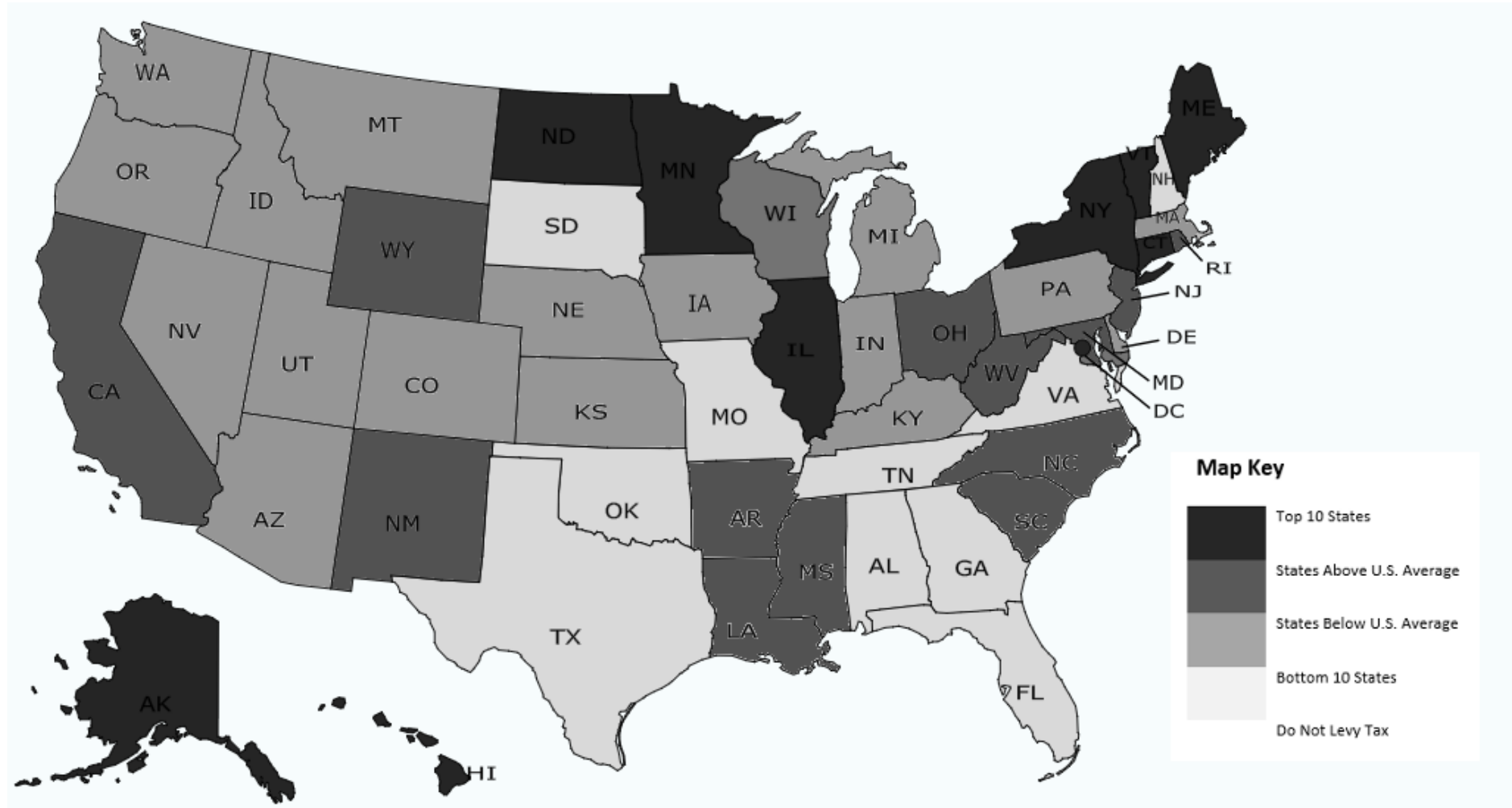
Total State and Local Tax Revenue

<u>Per Capita</u>					<u>Per \$1,000 Personal Income</u>			
<u>Year</u>	<u>U.S. Amount</u>	<u>Michigan Amount</u>	<u>Michigan as Percent of U.S. Average</u>	<u>Michigan's Rank</u>	<u>U.S. Amount</u>	<u>Michigan Amount</u>	<u>Michigan as Percent of U.S. Average</u>	<u>Michigan's Rank</u>
1983	\$ 2,847	\$ 3,213	113%	12th	\$ 225	\$ 263	117.0%	9th
1993	\$ 3,686	\$ 3,785	103%	14th	\$ 170	\$ 179	105.6%	13th
2008	\$ 4,731	\$ 4,096	87%	30th	\$ 115	\$ 114	99.3%	19th
2012	\$ 4,483	\$ 3,719	83%	34th	\$ 101	\$ 96	95.0%	32th
2013	\$ 4,599	\$ 3,750	82%	35th	\$ 103	\$ 96	92.5%	34th

Sources: Population data are from intercensal estimates by the U.S. Census Bureau obtained from the U.S. Bureau of Economic Analysis. Personal income data are from the U.S. Bureau of Economic Analysis.

Per capita amounts have been adjusted to 2013 dollars using the calendar year U.S. CPI-U.

State and Local Government Tax Revenue per \$1,000 of Personal Income as Percentage of U.S. Average, 2013

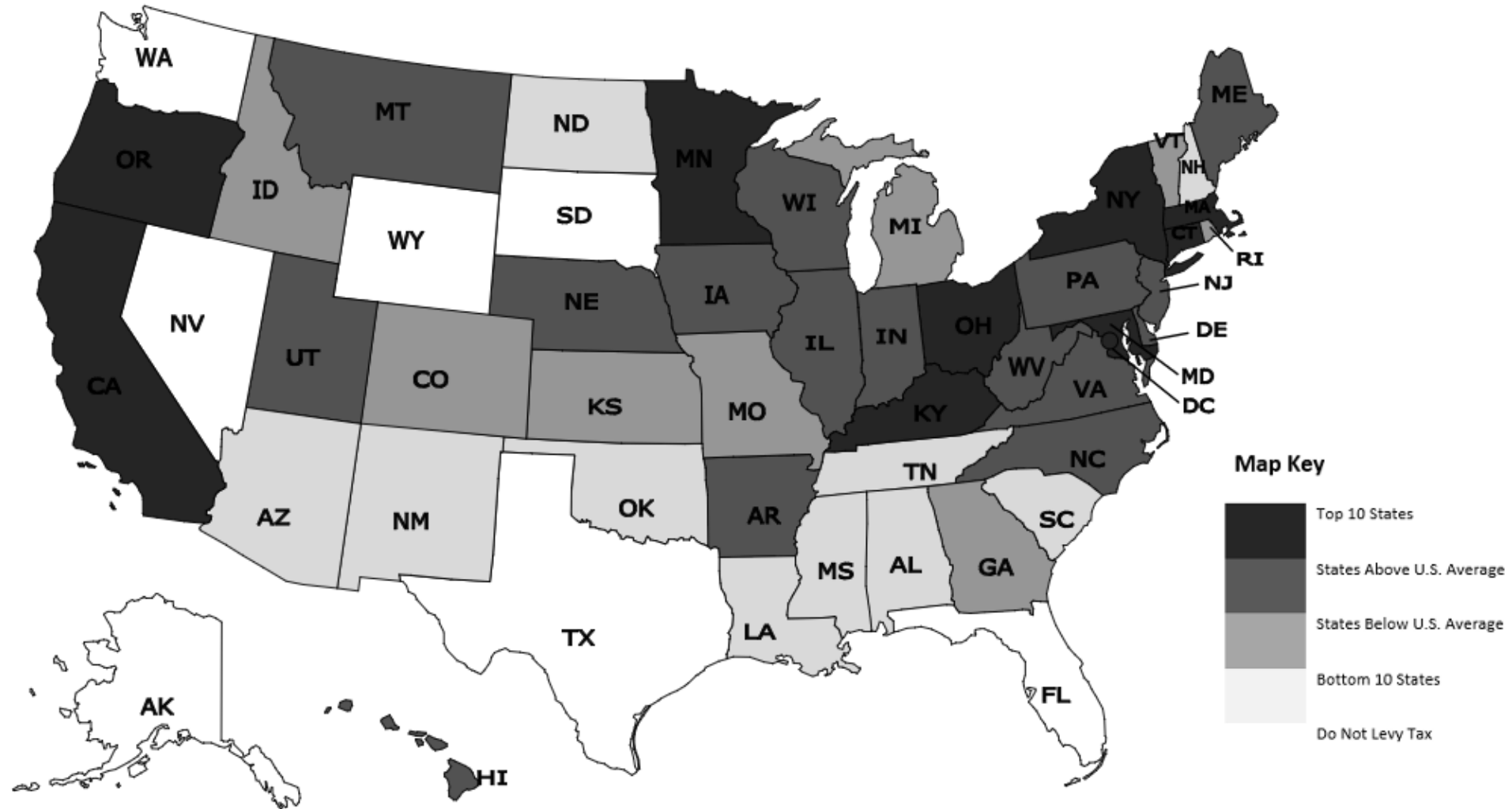


Is Michigan a “High Income Tax” State?

Individual Income Tax Revenues

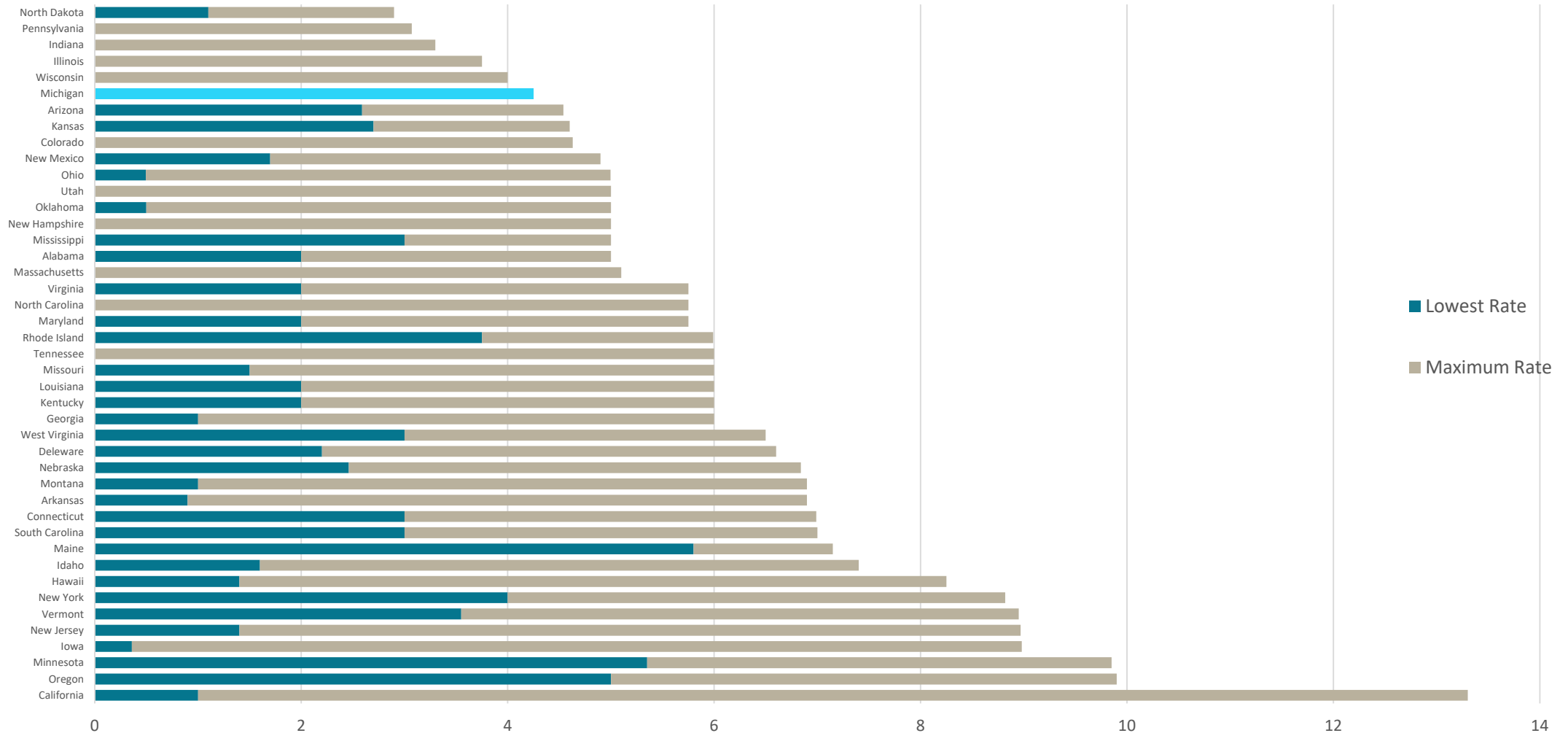
Year	U.S. Average		Michigan						
	Per Capita	Per \$1,000 Pers. Inc.	Per Capita			Per \$1,000 Personal Income			
			Amount	As % of U.S. Avg.	Rank	Amount	As % of U.S. Avg.	Rank	
1993	\$ 764	\$ 22	\$886	115.9	18 th	\$ 26	119.1	16 th	
2004	\$ 906	\$ 21	\$780	86.1	32 nd	\$ 20	92.0	34 th	
2008	\$ 1,085	\$ 24	\$831	76.6	34 th	\$ 21	87.9	34 th	
2012	\$ 992	\$ 22	\$754	76.0	34 th	\$ 19	87.0	34 th	
2013	\$ 1,069	\$ 24	\$866	81.0	34 th	\$ 22	91.8	34 th	
N/A - The U.S. Census Bureau did not segregate individual income and corporate income tax revenues in 1983.									
Source: U.S. Census Bureau, www.census.gov//govs/local/ .									

State and Local Government Individual Income Tax Revenue per \$1,000 of Personal Income as Percentage of U.S. Average, 2013



State Individual Income Tax Rates

(rate applied to bottom and top brackets)



Experience of other States

Model State/Local Tax System

Three Legged Stool

Not overly reliant on a single source of tax revenue

Three legs

1. Property Tax
2. Sales Tax
3. Income Tax



Distribution of Michigan State and Local Tax Revenues, Various Years

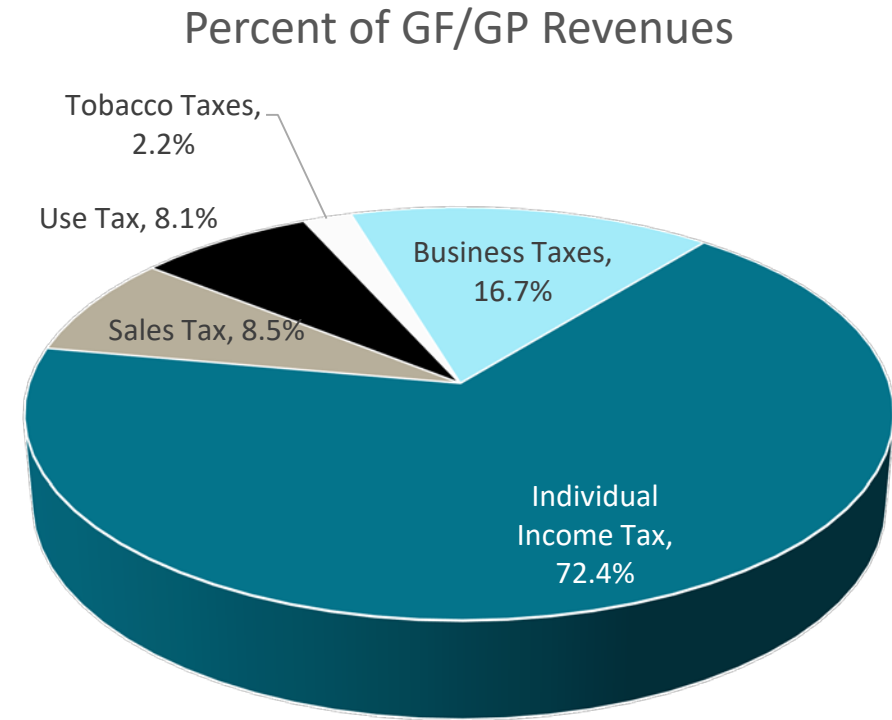
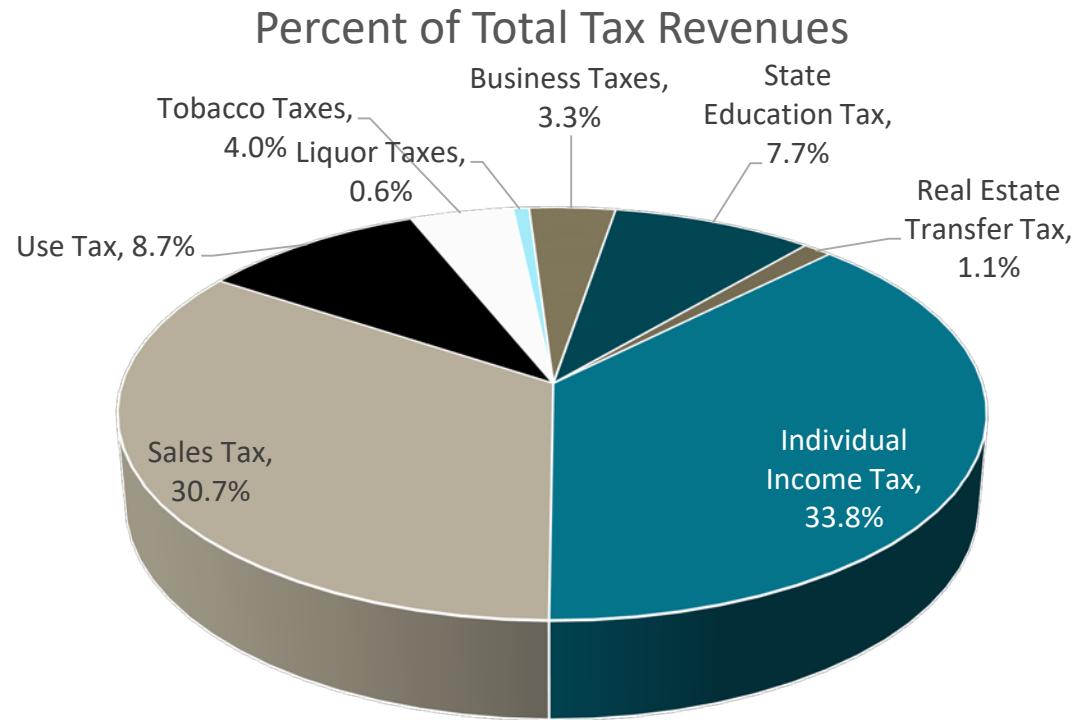
<u>Year</u>	<u>Property</u>	<u>Sales</u>	<u>Income</u>	<u>Other</u>
1993	41.29%	21.82%	31.63%	5.26%
2008	37.55%	32.38%	25.02%	5.05%
2012	36.65%	35.69%	22.50%	5.17%
2013	35.21%	33.87%	25.51%	5.41%
2013 U.S. Average	31.29%	34.11%	26.90%	7.70%
Source: U.S. Bureau of Economic Analysis and U.S. Census Bureau				

States without an Individual Income Tax

- Florida – tourism, 1/2 tax revenue from sales taxes
- Nevada – tourism, 3/5 tax revenue from sales taxes
- South Dakota – 1/2 tax revenue from sales taxes
- Texas – almost 1/2 tax revenue from sales taxes
- Washington – 3/5 tax revenue from sales taxes
- Alaska – Alaska Permanent Fund from oil extraction
- Wyoming – mineral extraction

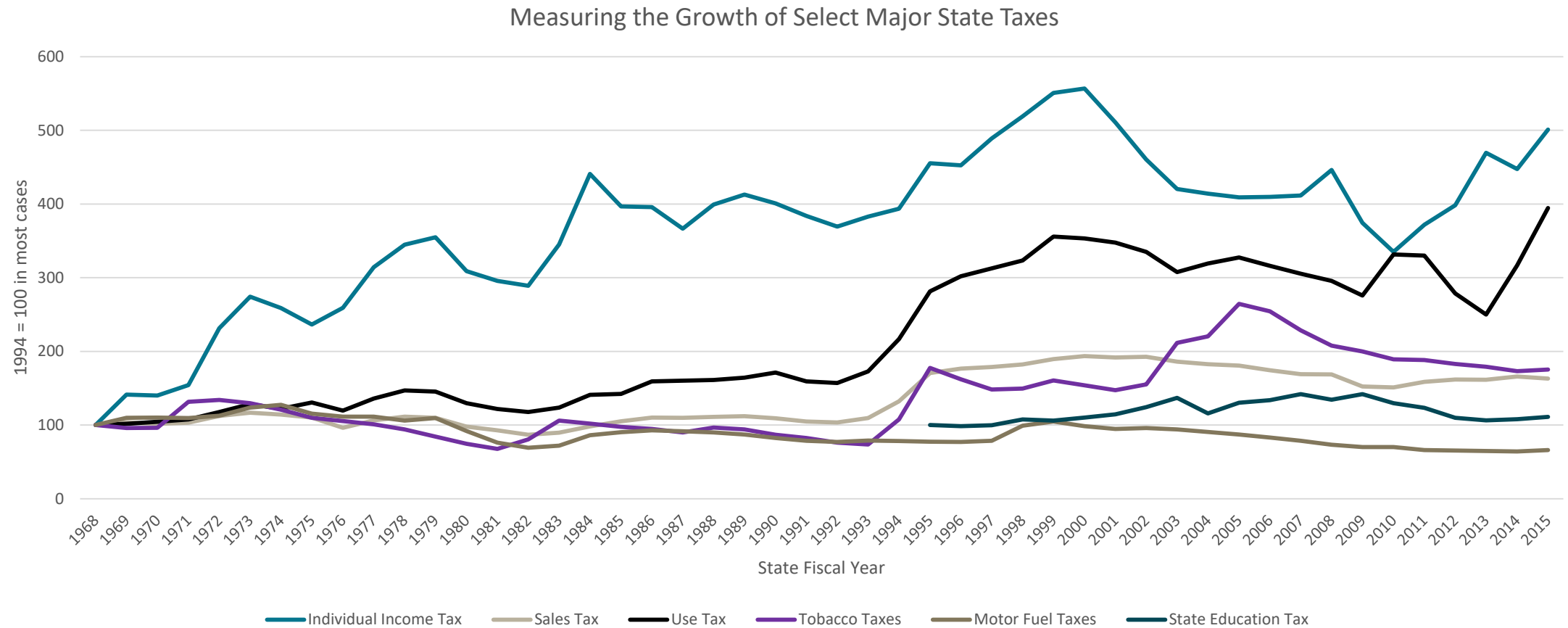
Role of Individual Income Tax in Michigan

Role Individual Income Tax Revenues Play in Funding Michigan Government

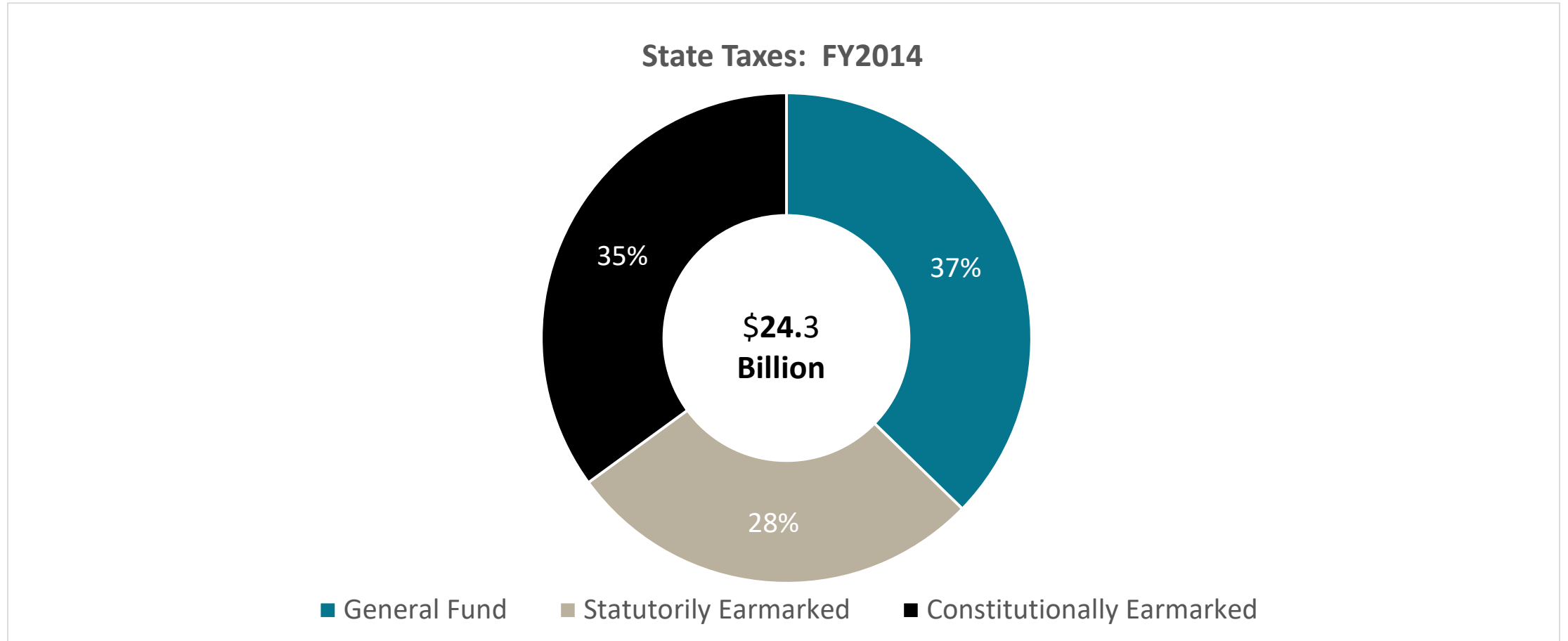


Source: 2014-15 Annual Report of the Michigan State Treasurer,
[www.michigan.gov/documents/treasury/State Treasurers Annual Report 2014-15 524479 7.pdf](http://www.michigan.gov/documents/treasury/State_Treasurers_Annual_Report_2014-15_524479_7.pdf)

Growth Pattern of Major State Taxes Since 1994



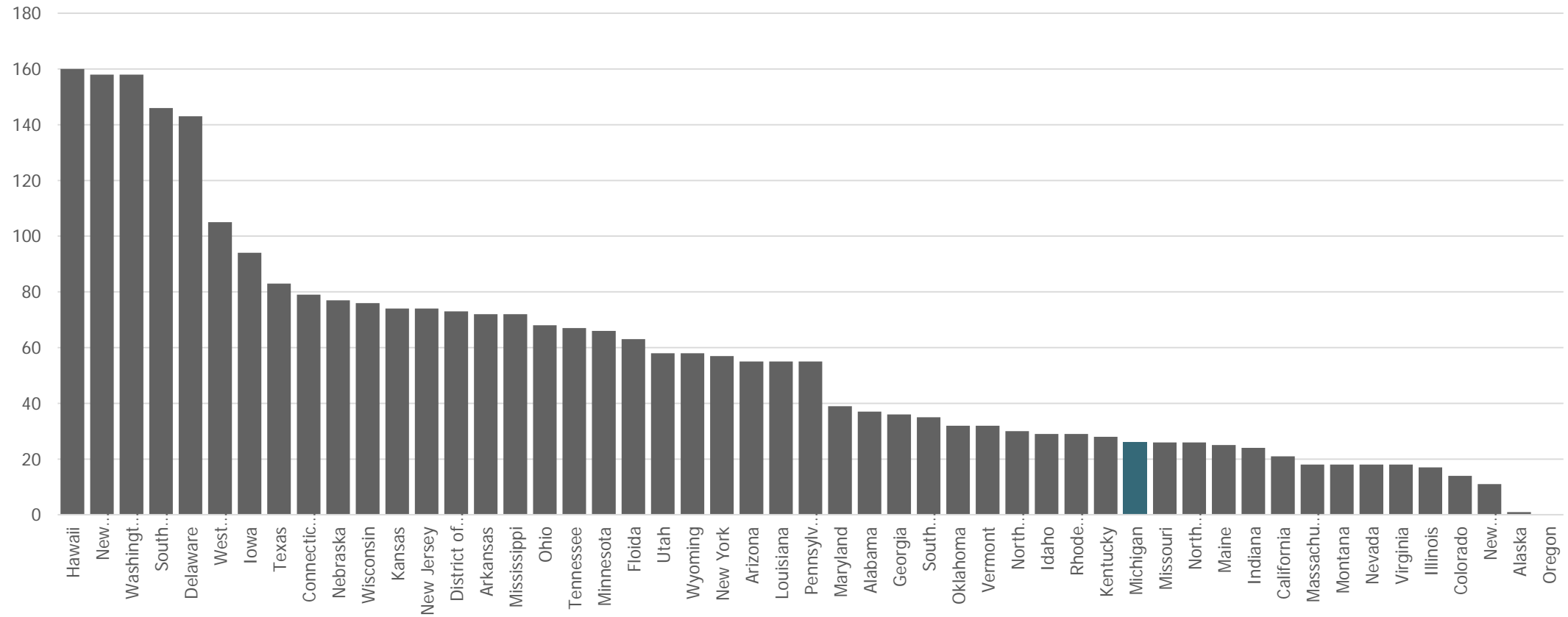
Nearly 2 of every 3 state tax dollar dedicated to a specific purpose



Options to Increase Tax Revenue

- There are two factors that determine how to increase tax revenue
- Factor one: what tax is levied?
 - Sales Tax
 - Property Tax
- Factor two: what mechanism is used to increase the revenue?
 - Increase the tax base
 - Increase the tax rate

State Taxes on Services, 2007



Service Taxes: Expanding the Tax Base

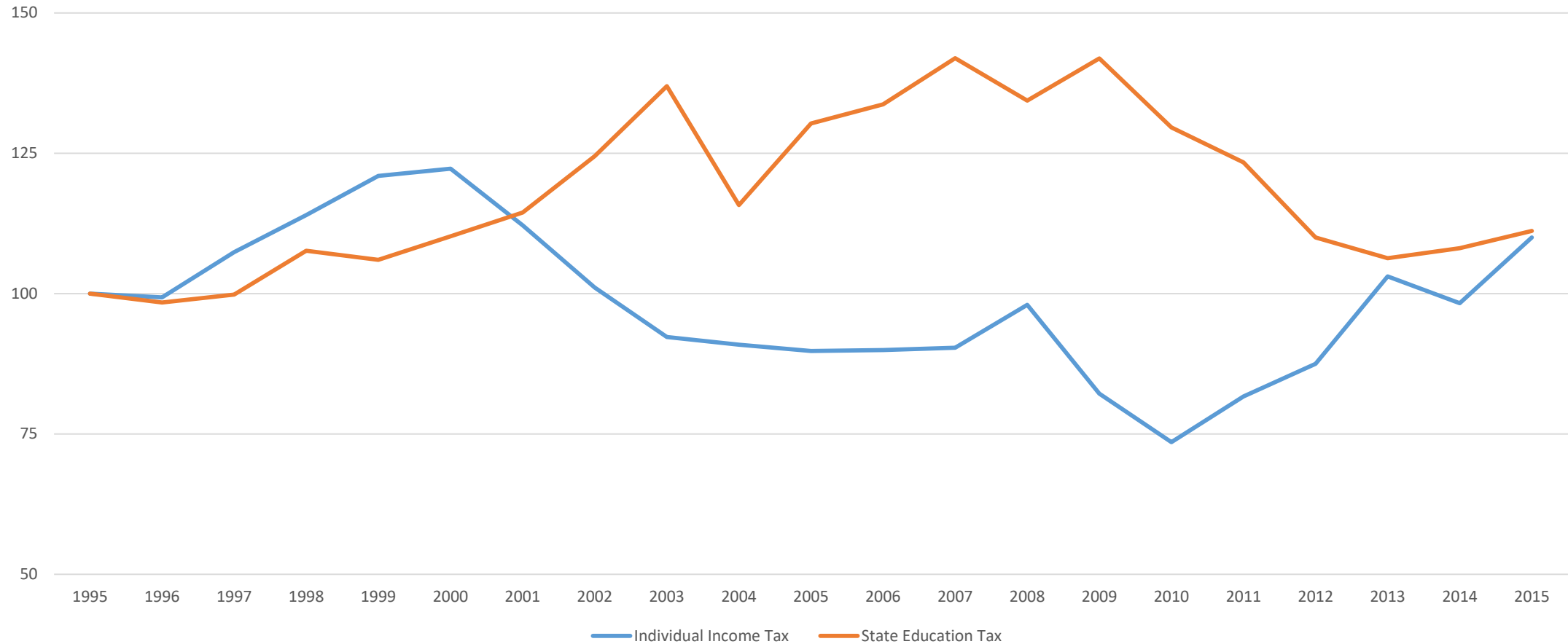
Increases from a Service Tax

- Potential \$12 billion in revenue
- Modernizes the tax code to reflect trends in spending
- Creates horizontal equity between services and goods

Existing Roadblocks

- Earmarking would apply to any expansion of the base
- Politically difficult – 2007 efforts demonstrate troubles
- Potential regressive effects of sales tax
- Requires a constitutional amendment

Growth of the State Education Tax



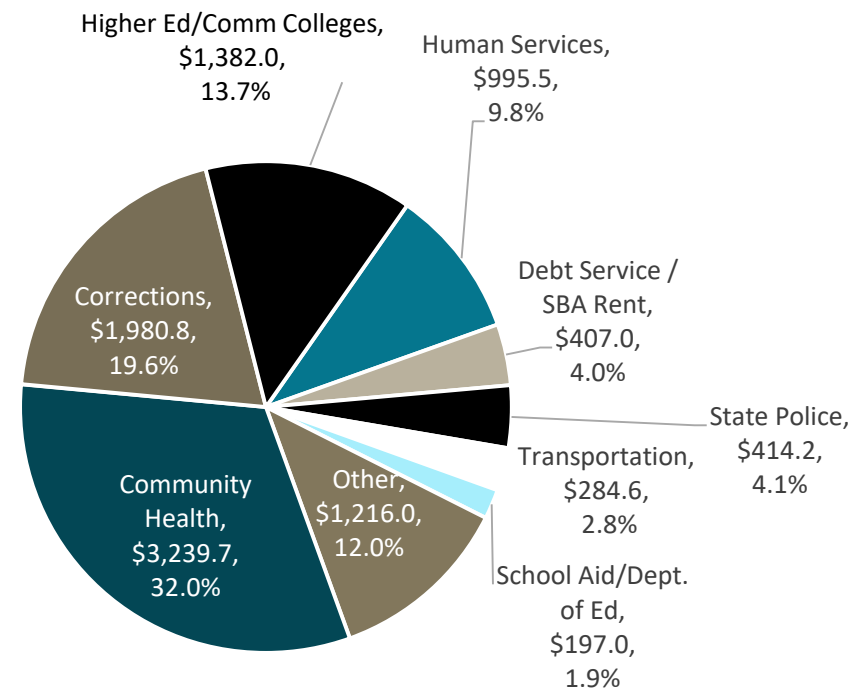
Increasing the Property Tax Rate

- A new tax would be needed
- The statewide tax base is small relative to revenue that would be lost to an income tax cut or elimination
- Would require a 30 mill levy to match income tax revenue
 - This would raise the highest rates over 100 mills, or 10% of taxable value
- Taxable value growth cap limits the potential of rate increases to 5% or inflation; severely limits the long-term potential of the property tax
- Could increase tax burden on lower income households

The Option of Spending Cuts

- The income tax raises 72% of the GF/GP budget
- Only 20% is spent by the state; only 11% on employee compensation
- 80% goes to local governments: school districts, counties, cities, etc.

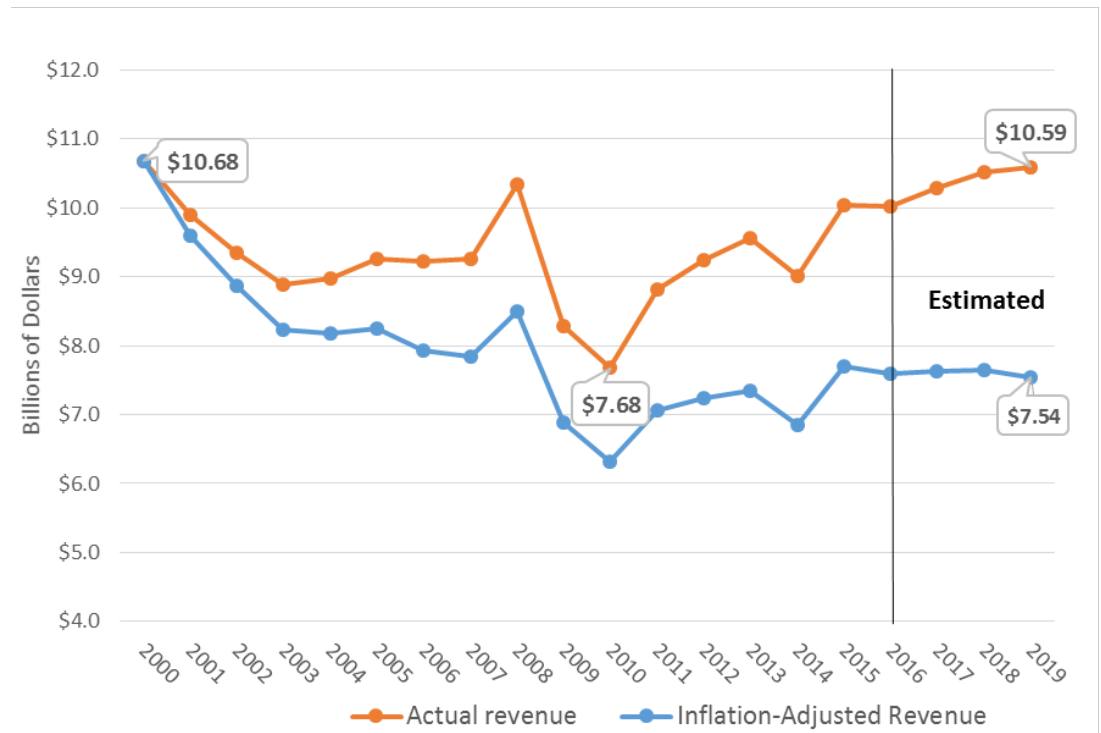
Distribution of General Purpose Revenue



Budget Challenges

- Federal matching means cuts can be more than 1:1
- GF/GP budget has been low
- Potentially \$2 billion a year in new spending and/or revenue decreases
 - Business Tax Credits, Highway funding, low income tax relief, healthcare spending, and more

GF/GP Revenue Growth from 2000-2019



Overall Outlook

- There are significant challenges facing the budget ahead
- Current trends do not show an increase in revenue from the current tax system as likely
- Increasing other taxes, while possible, would require constitutional amendments and compromise
- Cuts in the GF/GP budget would require a significant reduction in state service spending

Citizens Research Council of Michigan

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