



# Facts Matter

Facts Matter is a series of briefs highlighting Michigan's budget and tax system

## Income Tax:

- Only seven states have a flat tax
- 34 states and the District of Columbia have a graduated tax
- A graduated tax could help at least 90 percent of filers

## Income Tax: It's Time for the Flat Tax to Go

**F**or many years, Michigan has attempted to balance the state budget with one-time fixes, and budget cuts that:

- limit public safety, road repairs and other vital services; and
- fail to fix the structural deficit problem Michigan has faced for many years.

*One piece of a potential solution to this long-standing problem is changing Michigan's income tax from a flat tax to a graduated income tax.*

### Michigan's current income tax structure

Currently, Michigan taxes all personal income at a flat 4.35 percent. This rate will decline by 0.1 percent starting on October 1, 2011 and each October 1 for five years. By October 1, 2015, the income tax rate will be 3.9 percent. Due to Michigan's flat income tax, the state has not been capturing the growth in income that has been occurring among the state's higher-income taxpayers.

### What is a graduated income tax?

In a graduated income tax structure, such as the federal income tax, those with higher levels of personal income are in a higher tax bracket and are taxed at a higher rate and those with lower incomes pay a lower rate. Under such a tax structure, taxpayers in similar economic circumstances pay similar amounts of income tax. One example of a graduated income tax structure:

Tax Bracket	Taxable Income: Single	Taxable Income: Married, Filing Jointly
3.9%	\$0-\$20,000	\$0-\$40,000
4.35%	\$20,001-\$60,000	\$40,001-\$120,000
6.9%	\$60,001 and above	\$120,001 and above

## The fairness of a graduated income tax versus a flat tax

While everyone pays the same percentage of their income under Michigan's flat tax, that percentage represents a greater share of disposable income for low- to middle-income individuals and families and, therefore, results in a higher tax burden. For example:

- a married couple, filing jointly in Michigan with an income of \$40,000 pays a flat income tax of 4.35 percent, or \$2,175 a year;
- a married couple filing jointly in Michigan with an income of \$1,000,000 also pays 4.35 percent of their income in taxes as well, or \$43,500.

The percentage of income taxes paid by the second couple represents a much smaller share of their disposable income. In addition, the top bracket at 6.9 percent would put Michigan in about the middle of states with a graduated income tax:

- below California and Vermont at 10.3 percent and 9.5 percent respectively;
- above Arizona and Mississippi at 4.54 percent and 5 percent.

## A graduated income tax and revenue enhancement

Under a graduated income tax system, revenue growth would occur at a higher rate as income growth has been concentrated among groups earning higher incomes, thus creating a more stable and adequate source of revenue for the state to provide necessary services to its residents.

The graduated income tax example used on the previous page would yield an additional \$600 million in revenue, and more in the future in response to income growth.

## Previous attempts to implement a graduated income tax

To move to a graduated income tax in Michigan, a majority of voters must vote to amend the state Constitution, as it currently prohibits a graduated income tax system. The question has been put to voters on multiple occasions (1968, 1972 and 1976) and has failed.

Recent polling suggests that public attitudes about a graduated income tax could be changing:

- A poll taken in May 2009 found that 60 percent of Michigan voters surveyed now favor a graduated income tax to replace the state's flat tax, while 33 percent are opposed. The poll was conducted by EPIC-MRA of Lansing;
- A Detroit News/WXYZ poll conducted in June, 2007 by EPIC-MRA found that 57 percent of those polled favored a graduated income tax;
- A Detroit Free Press/Channel 4 poll conducted in July and August 2007 by Iowa-based Selser & Co. found that 53 percent favored a graduated structure;
- Michigan State University's 2008 State of the State Survey also confirmed public support for a graduated income tax, with 57.2 percent of those polled in favor.