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On March 29, 1983 Governor James Blanchard approved a 38% increase in the state's personal income tax. The tax increase is retroactive to January 1, 1983, and raises the income tax from 4.6% to 6.35%. This 1.75 percentage point increase includes a basic income tax increase of 1.5 percentage points plus a 0.25 percentage point increase dedicated to eliminating Michigan's $800 million of inherited debt, bringing the state's accounting practices into conformity with generally accepted accounting practices and easing cash flow problems. The surcharge would expire no later than September 30, 1986.

The tax increase would be phased out according to the following schedule. The listed rates include the 0.25% surcharge:

1983--6.35%
1984--no more than 6.1%
1985--no more than 5.35%
1986--no more than 5.35%
1987--no more than 5.1%

The preceding rates are maximums. The tax rate would revert to 4.6% only if and when the state's unemployment rate fell below 9%. The tax increase is also indexed to the state unemployment rate and could decline more rapidly if unemployment dropped quickly. The income tax rate would fall to 3.9% if state unemployment declined to under 7%.

For purposes of determining the income tax rate, unemployment will be computed by averaging the seasonally adjusted unemployment rate for the two quarters spanning April to September. Unemployment would have to decline to 14.5% before phase-out of the increase was started. Effective January 1 of the following year the tax rate will be reduced by 0.1 percentage point for each 0.5 percentage point decline in this derived unemployment rate. If the formula relating unemployment to the income tax rate yielded a more rapid rate of decline than listed in the calendar schedule, the state would adopt whichever technique provided the lower income tax rate. The tax rate could be reduced in proportion to declines in unemployment but could not be increased even if unemployment resumed its upward climb.

The newly approved legislation made the 6.35% income tax rate retroactive to January 1, 1983. However, since the withholding rate for this period was 4.6%, in order for the withholding rate for the year to average 6.35%, the effective rate for the remainder of this year must be correspondingly higher, 6.92% starting April 1.

Passage of the income tax increase does not guarantee that the state will have the requisite funds to meet its financial obligations in a timely manner this year. Although major employers should begin to withhold at the higher rate starting in April, significant additional funds will not begin to flow into the state's treasury until at least mid-May. As a result, the state will continue to experience serious cash flow problems for the remainder of the 1983 fiscal year. This will necessarily require the state to continue for another year the deferrals and accounting practices it has pledged to eliminate.

Revenue generated by the 0.25% income tax surcharge will be deposited into the newly created State Accounting and Fiscal Responsibility Account. When sufficient revenues are available to fund accounting procedure revisions, a transfer would be made to the state's general fund from the accounting and fiscal responsibility account to effect these revisions. Programs affected by these accounting revisions include Medicaid, general assistance medical, and the voluntary heating fuel assistance program for social service recipients.

The following table details the amount of revenue we project will be generated by the personal income tax increase for fiscal years 1983-1986. (All figures are in millions of dollars.)

| Fiscal Year | Projected Yield from 4.6% Tax | Tax Increase | 0.25% Surcharge | Total |
|---|---|---|---|---|
| 1983 | $ 2,625 | $ 675 | $112 | $ 3,412 |
| 1984 | $ 2,800 | $ 825 | $157 | $ 3,782 |
| 1985 | $ 3,235 | $ 358 | $179 | $ 3,772 |
| 1986 | $ 3,620 | $ 403 | $202 | $ 4,225 |
| 4-yr total | $12,280 | $2,261 | $650 | $15,191 |

Note: The table provides income tax revenue projections only and does not estimate yields for all sources of general and restricted fund revenues. These projections are based on the tax rates provided in the calendar schedule detailed on page 1.