

PUBLIC POLICY ADVISOR

The Michigan Sales Tax: Reconsidering Its Role in a Balanced Tax System

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INTRODUCTION

The sales tax is the largest revenue source for state governments. In 1991 nearly one-third of all state government revenue came from general sales and gross receipts taxes, including use taxes, despite the fact that only 45 states levy such taxes. Of these 45 states, 13 raised more than 40 percent of their revenue from the sales tax.

The sales tax has several advantages over competing taxes: It raises large amounts of revenue at low rates; it has a broad base, which allows for stability even during weak economic times; a portion of the tax is paid by visitors, thus lowering residents' tax burdens; and it is better received by the public than either income or property taxes. (The last aspect has less to do with the sales tax being perceived as a "fair" tax and more to do with its low profile; consumers pay the tax in small amounts over the course of the year, rather than making large monthly or annual payments.)

The sales tax has its drawbacks, too: It is regressive, taking a larger percentage of poor households' income than large households' income; it distorts economic behavior by causing businesses and households to consume nontaxed items over taxed items; and in many states, there are numerous exemptions and exceptions to the tax, making business compliance and government administration difficult.

Michigan currently levies a constitutionally set 4 percent sales tax on the retail sale of tangible goods. The state also levies a 4 percent use tax on the storage, use, and consumption of tangible goods (if they escape the sales tax) and on some services, including hotel and motel accommodations. Michigan law narrowly defines the sales and use tax base to exclude some goods and almost all services. Furthermore, the law prohibits local governments from levying additional sales taxes, although the state must transfer 15 percent of sales tax revenue to local governments.

These legal restrictions help to explain why Michigan ranks near the bottom among all states in comparisons of sales tax effort, per capita revenue, and revenue as a percentage of personal income.

BACKGROUND AND LEGISLATIVE HISTORY

In 1932 Mississippi passed the nation's first sales tax. One year later, Michigan Public Act (PA) 167 of 1933 established a general sales tax of 3 percent on retail sales of tangible goods. It exempted only sales for resale, sales to government units, and services. Beginning in 1935 and continuing through the present, various legislative acts have diminished the base, and thus the revenue raising potential, of the sales tax. The only exception to this trend was the 1960 constitutional amendment that raised and fixed the sales tax rate at 4 percent beginning in 1961.

PA 94 of 1937 established a 3 percent use tax to be applied to the storage, use, and consumption of tangible goods and services that were not subject to the sales tax. This included goods that were purchased in other states for use in Michigan. The original list of exemptions mirrored the list of goods exempted from the sales tax, and subsequent legislation added to this list; however, the legislature on occasion has broadened the use tax base. Specifically, in 1959 PAs 263 and 272 imposed the use tax on hotel and motel accommodations and intrastate telecommunications charges, respectively. The use tax rate was increased to 4 percent in 1960, and while it is not constitutionally fixed, state legislators have not since changed the rate.

Another important distinction between sales and use taxes was created by the Sales Tax Diversion Amendment of 1946. This amendment began the practice of allocating sales tax revenue among the state general fund, local governments, and schools. The amendment did not cover the use tax, so all use tax revenue continued to go directly to the state general fund. Currently, sales tax revenues are allo-

cated as follows: 60 percent goes to the school aid fund, 15 percent to local governments, and 25 percent to the general fund. Of the general fund portion, at least 27.9 percent of the tax derived from auto-related items must go to the transportation fund. Exhibit 1 presents a chronology of the major legislative actions affecting the sales and use taxes.

SALES TAX REVENUE HISTORY

The previous section highlighted the legislative actions that have altered the sales tax base over time. Most of these changes have had only a minor effect on sales and use tax revenues; however, the cumulative effect of all exemptions has been quite signifi-

cant (see section on tax expenditures). Exhibit 2 presents a 15-year history of the sales tax. (Henceforth, we will refer to combined sales and use taxes as the sales tax.)

In nominal terms, sales tax revenues grew annually from 1978 to 1992, except for 1982 and 1991 when revenues declined slightly. The downturns coincided with recession years, which are generally associated with a decline in retail sales, the main base of sales tax revenue. In particular, autos, building materials, and furniture—which make up about 37 percent of the sales tax base—are highly income elastic, meaning that their sales decline significantly

EXHIBIT 1: Legislative History of the Michigan Sales and Use Taxes

1933	Public Act 167 establishes the general sales tax, exempting only sales to the federal and state governments and sales for resale.
1935	Exemption granted for tangible personal property used in industrial processing or farm production. Sales to nonprofit organizations are also exempted.
1937	Public Act 94 establishes the use tax, exempting property already subject to the sales tax, property exempt from taxation under federal or state law, and property temporarily taken into the state by a nonresident.
1939	Exemption from the sales tax of transactions involving commercial vessels.
1946	Passage of the Sales Tax Diversion Amendment establishes a system of allocating sales tax revenue to the general fund, local governments, and the school aid fund.
1950	Sales tax exemption for newspapers, periodicals, and motion pictures.
1952	Exemption from the sales tax of sales to commercial radio and television station operators.
1955	Exemption from the sales tax of sales of vehicles purchased in Michigan for use out of state.
1959	Use tax levied on intrastate telecommunications and on hotel and motel accommodations.
1960	Constitutional amendment raises the sales tax from 3 to 4 percent; use tax also raised to 4 percent.
1974	Constitutional amendment exempts prescription drugs and food for home consumption.
1978	Exemption from the sales tax of hearing aids, ophthalmic aids, and orthopedic aids and equipment to assist the disabled. Exemption for components of air and water pollution control facilities.
1983	Use tax amended to include tax on personal property modified and affixed to real estate by construction contractors.
1985	Exemption for computers used in industrial processing.
1986	Exemption of sales to businesses engaged in high technology activity located in "enterprise zones."
1987	Sales tax imposed on new or modified computer software for general sale; custom software exempted. Exemption for bottled water and items purchased with food stamps.
1989	Use tax exemption for agricultural land titles, portable grain bins, and equipment used in commercial fishing.
1990	Exemption from the sales tax of qualified new vehicle sales, and sales of used vehicles to insurance companies to settle claims.
1992	Use tax exemptions for oxygen used as a prescription drug and sale of parts affixed in Michigan to commercial aircraft.

SOURCES: Michigan Department of Treasury, *Analysis of Michigan's Sales Tax, FY 1988-89*, October 1992, and Citizens Research Council of Michigan, *Outline of the Michigan Tax System*, May 1991 and 1993.

EXHIBIT 2: Michigan Sales Tax Revenue, FY 1977-78 to FY 1991-92

Fiscal Year	Nominal Sales Tax Revenue	Nominal Total State Tax Revenue	Nominal Property Tax Revenue	Detroit CPI	Real Sales Tax Revenue (1982-84 dollars)	Personal Income	Sales Tax as % of Personal Income	Sales Tax as % of Total State Taxes	Sales Tax as % of State + Property Taxes	Property Tax as % of State + Property Taxes
1978	\$1,587	\$5,376	\$3,207	65.3	\$2,430	\$80,405	1.97%	29.5%	18.5%	37.4%
1979	1,726	5,973	3,485	73.6	2,345	88,554	1.95	28.9	18.2	36.8
1980	1,742	5,925	3,889	85.3	2,042	94,080	1.85	29.4	17.8	39.6
1981	1,824	6,111	4,411	93.2	1,957	100,082	1.82	29.8	17.3	41.9
1982	1,822	6,207	4,898	97.0	1,878	101,228	1.80	29.4	16.4	44.1
1983	1,946	6,997	5,173	99.8	1,950	107,437	1.81	27.8	16.0	42.5
1984	2,234	8,521	5,187	103.2	2,165	118,047	1.89	26.2	16.3	37.8
1985	2,447	8,751	5,374	106.8	2,291	127,250	1.92	28.0	17.3	38.0
1986	2,647	9,202	5,593	108.3	2,444	136,040	1.95	28.8	17.9	37.8
1987	2,736	9,235	5,851	111.7	2,449	142,337	1.92	29.6	18.1	38.8
1988	2,880	10,062	6,215	116.1	2,481	152,271	1.89	28.6	17.7	38.2
1989	3,046	10,804	6,761	122.3	2,491	163,269	1.87	28.2	17.3	38.5
1990	3,161	10,974	7,391	128.6	2,458	171,003	1.85	28.8	17.2	40.2
1991	3,145	10,902	7,998	133.1	2,363	174,750	1.80	28.8	16.6	42.3
1992	3,205	10,930	8,639	136.0	2,357	184,089	1.74	29.3	16.4	44.1

SOURCES: Michigan Department of Treasury, *Annual Report of the State Treasurer*, various years, and Citizens Research Council of Michigan, *Outline of the Michigan Tax System*, various years. Calculations by Public Sector Consultants, Inc.

NOTE: Sales tax figures refer to sales tax plus use tax. All revenue figures are in millions.

during recessionary periods, increasing the instability of the sales tax base. Real sales tax revenue (1982-84 dollars) has been more cyclical than nominal revenue, declining from 1978 until 1982, rising from 1983 until 1989, and declining again from 1990 until the present. The peak real revenue figure from 1989, \$2.49 billion, only slightly exceeded the 1978 figure of \$2.43 billion.

The sales tax as a percentage of personal income followed a cyclical path similar to real tax revenue, with the most recent data point in 1992 at a 15-year low of 1.74 percent. This series indicates that the sales tax may be declining in its ability to produce revenue for the state. In contrast, when we turn our attention to sales tax revenue in relation to all state tax revenue—which includes sales, income, business, inheritance, cigarette, alcohol, and gasoline excise taxes—we find that the sales tax share remained about 28 to 29 percent of total state taxes throughout the period, an indication that the sales tax is doing no worse than most other state revenue sources. Likewise, if we look at sales tax revenue as a percentage of all state taxes plus local, general

property tax revenue, we find that the sales tax share has remained steady between about 16 and 18 percent, although it has declined in recent years.

It is useful to place the historical performance of the sales tax within the broader context of the entire Michigan tax system. Conventional wisdom holds that income, sales, and property taxes should each raise 20 to 30 percent of all revenue in a well balanced state and local tax system, yet Michigan has consistently underused its sales tax and overused its property tax. In recent years while the sales tax share has dipped to its current low of around 16 percent, the local property tax share has climbed to more than 40 percent of total tax revenue. The state legislature's elimination of school based property taxes provides an opportunity to address this growing imbalance. If Michigan opts for a more balanced system, one possibility would be to raise the sales tax rate and use the additional revenue to replace some of the lost property tax revenue.

Exhibit 3 illustrates how the tax balance would improve if Michigan raised the sales tax rate and

EXHIBIT 3: Improving Tax Balance by Increasing Sales Tax to Replace Property Tax
(actual and estimated values based on FY 1991-92)

	Actual	Estimated	
		5%	6%
Tax rate	4%	5%	6%
Revenue (in millions)			
Sales tax	\$3,205	\$4,006	\$4,808
Total state tax	10,930	11,731	12,533
General property tax	8,639	7,838	7,036
Total state + property tax	\$19,569	\$19,569	\$19,569
Percent of combined total			
Sales tax	16.4%	20.5%	24.6%
Property tax	44.1%	40.1%	36.0%

SOURCE: Public Sector Consultants, Inc.

diverted the additional revenue to replace school-based property taxes. A sales tax rate of 6 percent would raise an extra \$1.6 billion, increasing the sales tax share of total revenue to almost 25 percent and lowering the general property tax share to about 36 percent.

SECTORAL REVENUE AND ELASTICITIES

Another way to measure the revenue-producing performance of the sales tax is to compare how various components have changed relative to changes in personal income (measured in percentage terms). This measurement, known as the income elasticity of the sales tax, helps us evaluate the ability of different economic sectors to raise revenue over time. An elasticity equal to one indicates that sales tax collections will increase one percent for every one percent increase in personal income. An elasticity in excess of one means that sales tax collections will increase by more than one percent for every one percent increase in personal income. Exhibit 4 shows that total sales tax collections increased about 75 percent and personal income increased about 82 percent for the ten-year period between 1982 and 1992 resulting in an income elasticity of .92.

Sales tax growth relative to personal income was not even across sectors; revenues from building and hardware, furniture, and vehicle sales grew much faster than personal income. Much of the retail sector, which provides the bulk of sales tax revenues, grew 80 to 90 percent as fast as personal income (elasticities between .8 and .9), and the nonretail sectors grew even slower. The service sector showed the sharpest increase in revenue relative to

income; however, growth in business services, a major service component, occurred in large part because of the addition of computer services to the tax base. Revenue from medical and health services grew 45 percent faster than income, reflecting the rapid expansion of this sector, most of which is exempt from taxation. These data indicate that expanding the sales tax to include health services could generate substantial future revenue.

TAX BURDENS: CONSUMERS, BUSINESSES, AND TOURISTS

We can also examine the sales tax's role in the Michigan tax system by looking at how different groups share the sales tax burden and by comparing sales tax burdens to other tax burdens (i.e., property tax). Three general groups worth looking at separately are in-state consumers, businesses, and tourists.

Sales taxes are intended to be a tax on in-state consumption. Therefore, we expect that in-state consumers will bear the bulk of the sales tax burden through their purchases of food, clothes, furniture, automobiles, other retail goods, and taxed consumer services. The business share of the sales tax burden results from business purchases made in nonretail sectors, including agriculture, mining, construction, manufacturing, business services, and wholesale, as well as from retail purchases of business vehicles, utilities, building supplies, and business-related lodging and meals. Sales tax collections in these areas added up to an estimated 27 percent of all sales tax collections for FY 1992. In arriving at this figure, we assumed that businesses made between

EXHIBIT 4: Sales Tax Revenue and Income Elasticities for Selected Sectors

Sector	Sales and Use Tax Revenue (in thousands)			Percent Change		Elasticities	
	FY 1977	FY 1982	FY 1992	1982-92	1977-92	1982-92	1977-92
Manufacturing	\$83,250	\$111,171	\$199,373	79.3%	139.5%	0.97	0.90
Transportation, comm., and util.	146,077	246,798	358,957	45.4	145.7	0.56	0.94
Telephone	40,727	65,760	109,389	66.3	168.6	0.81	1.08
Electric and gas	101,265	173,783	225,230	29.6	122.4	0.36	0.79
Wholesale trade	48,801	77,146	94,237	22.2	93.1	0.27	0.60
Retail trade							
Building and hardware	90,268	90,052	181,093	101.1	100.6	1.24	0.65
General merchandise	146,551	178,528	295,422	65.5	101.6	0.80	0.65
Major dept. stores	84,466	96,884	139,201	43.7	64.8	0.53	0.42
Variety stores	41,278	58,201	80,298	38.0	94.5	0.46	0.61
Food	84,386	118,806	199,794	68.2	136.8	0.83	0.88
Automotive	363,971	416,659	742,697	78.3	104.1	0.96	0.67
New and used car dealers	256,606	240,360	495,441	106.1	93.1	1.30	0.60
Gasoline stations	78,786	139,808	176,253	26.1	123.7	0.32	0.80
Apparel	56,848	70,500	121,447	72.3	113.6	0.88	0.73
Furniture	55,108	65,740	128,480	95.4	133.1	1.17	0.86
Eating and drinking places	102,502	144,721	251,036	73.5	144.9	0.90	0.93
Misc. retail stores	110,250	149,767	252,352	68.5	128.9	0.84	0.83
Services	63,342	98,724	230,399	133.4	263.7	1.63	1.70
Hotels	14,133	19,748	41,193	108.6	191.5	1.33	1.23
Misc. business	15,237	30,718	88,573	188.3	481.3	2.30	3.09
Health and medical	1,990	2,594	5,679	118.9	185.4	1.45	1.19
TOTAL	\$1,390,095	\$1,823,314	\$3,188,943	74.9%	129.4%	0.92	0.83
Total personal income (in millions)	\$72,032	\$101,228	\$184,089	81.9%	155.6%		

SOURCE: Revenue figures from Michigan Department of Treasury. Calculations by Public Sector Consultants, Inc.

90 and 95 percent of nonretail purchases and between 5 and 10 percent of retail purchases, with larger shares assumed for motor vehicles and utilities.

In addition to paying about 27 percent of the sales tax, businesses pay about 35 percent of local property taxes. The recent property tax cut relieves businesses of a significant share of their tax burden. If the legislature decided to replace all lost property tax revenue with an increased sales tax, businesses would come out net winners because they would pay about 8 percent less in sales tax than they currently pay in property taxes. Therefore, businesses will benefit by any exchange of sales tax for property tax.

When possible, states attempt to relieve in-state consumers' tax burdens at the expense of visitors through a process known as tax exporting. Tax exporting can involve levying higher sales and use tax rates on hotels, motels, and rental cars or taxing

amusements frequented by tourists. Florida, Hawaii, and Nevada all export significant shares of their sales tax bases. Michigan has some sales tax exporting opportunities as well.

Data from the Michigan Department of Treasury for FY 1992 show that guest accommodations, hotel dining, and car rentals raised more than \$61 million in sales and use tax revenue. We assume that all of this tax was paid by visitors.¹ Retail eating and drinking establishments raised more than \$251 million; retail apparel, accessories, and major department stores generated \$271 million; and gas stations brought in \$176 million in sales and use taxes. If we assume that visitors make between 5 and 10 percent of these purchases, then between \$96 million and \$131 million of the \$3,205 million (refer to Exhibit

1 Some of these expenses are undoubtedly paid by Michigan residents, but we assume that tourists bear this entire burden to compensate for tourist spending in other areas of the state economy not captured by our estimate.

2) in sales taxes are exported. This works out to be 3 to 4 percent of the sales tax base; hence, exporting does not appear to be a significant advantage for Michigan.

SALES TAX EXPENDITURES

We cannot discuss a tax's declining ability to produce revenue without mentioning tax expenditures. In the case of the sales tax, tax expenditures relate directly to specified exemptions; for every dollar of exempted goods or services sold, the state forgoes 4 cents in revenue. Exhibit 5 presents a list of the largest exemptions and their percentage share of total sales tax expenditures. The \$2.4 billion of sales tax expenditures equal 75 percent of sales tax revenue; put another way, 43 percent of the potential tax base (revenue plus expenditures) currently goes untaxed.

Almost half of the expenditures are due to the exemption of services from the tax base; food and goods purchased for use in industrial processing account for 20 and 14 percent of expenditures, respectively. Good arguments can be made for keeping exemptions for all three of these categories: Taxing food places a disproportionate burden on low-income families; taxing industrial processing increases the cost for consumers who will pay tax on the finished goods (tax pyramiding); and taxing in-

state services may cause consumers to purchase services from multistate (out-of-state) providers and subsequently not pay a use tax.

While these arguments should be given serious consideration, there are good reasons to end exemptions for food and services. In the case of food, low-income families account for a relatively small share of the consumption base. An income-dependent tax credit for sales tax paid on food can correct for the tax's regressivity and simultaneously raise substantial revenue from the relatively well-to-do majority of taxpayers. While this approach has worked in many states, Michigan voters would need to overturn the constitutional amendment exempting food before implementing a credit. Such changes would likely face formidable political opposition.

As the economy has become more service oriented, people have spent more money on services and less on goods. This trend shows no signs of slowing;² if the tax-exempt status of services continues, sales tax expenditures will contribute to the decline in the sales tax share of total tax revenue and create further imbalance in Michigan's tax system. While the problem of taxing sales from multistate

² For a more detailed treatment of expanding the sales tax to include services see the July 1992 *Public Policy Advisor* entitled "Cashing in on a Service Economy: Expanding the Sales Tax."

EXHIBIT 5: FY 1991-92 Sales Tax Expenditures

Category	Tax Expenditure (in thousands)	Percent of Total
Sales to governments, churches, and nonprofit organizations	\$37,713	2%
Services	1,189,910	49
Newspapers, periodicals, and films	25,177	1
Farm production	46,728	2
Industrial processing	339,423	14
Food for home consumption	474,149	20
Prescription drugs	20,660	1
Pollution control facilities	39,632	2
Interstate sales	77,608	3
Interstate telecommunications	40,990	2
Custom computer software and support	27,327	1
Other	89,514	3
Total expenditures	\$2,408,831	100%
Total revenue	\$3,205,000	
Expenditures as a percent of revenue	75%	

SOURCE: State of Michigan, *Executive Budget, Tax Expenditure Index FY 1991-92*.

service providers will remain, a sales tax on services will end some of the distortions in economic behavior that encourage the consumption of nontaxed services over taxed goods and translate into a competitive advantage for service providers over goods providers.

The elimination of all food and service tax expenditures could raise more than \$1.66 billion at the current 4 percent tax rate. Recall from Exhibit 3 that raising the tax rate to 6 percent and maintaining the current tax base produced only \$1.6 billion. A combination of raising the tax rate and cutting tax expenditures could be a potent revenue raiser; however, ending the food exemption and raising the statutory rate both would require amending the state constitution.

INTERSTATE COMPARISONS

It can be informative to compare the performance of the sales tax not only to that of other taxes within the Michigan tax system, but also to other states' sales tax performance. Exhibit 6 compares the Michigan sales tax to that of the other 44 states levying a sales tax. The most visible basis of comparison is the tax rate. Of the states levying a state or local sales tax, thirteen, including Michigan, levy a state tax rate less than or equal to 4 percent. When local sales taxes are factored in only four states, including Michigan, remain at or below 4 percent. Note that not all local governments tax at the maximum combined rate in the states that permit local sales taxation, so select localities in some states may also remain below the 4 percent threshold.

Michigan consumers not only pay the lowest combined rate, but they experience the fifth lowest sales tax burden when measured in terms of both tax per capita and tax as a percentage of personal income. (If we include Alaska, where there are only local sales taxes, Michigan has the sixth lowest burden of all states levying general sales taxes.) Michigan sales tax collections equal 1.87 percent of personal income, well below the 5.90 percent paid by residents of the state of Washington but only slightly more than the 1.27 percent Vermont residents pay. On a per capita basis, Michigan's \$341 falls much closer to Vermont's low, \$222, than Hawaii's high, \$1,127. Incidentally, when selective sales taxes are included in these tax burden compilations, Michigan ranks 45 out of 50. No neighbor-

ing Great Lakes state ranks below Michigan in any of these categories. Likewise, each of these neighboring states uses the sales tax to raise a greater share of total state taxes (excluding local property taxes) than does Michigan.

The Advisory Commission on Intergovernmental Relations (ACIR) publishes two indexes that allow comparisons of state tax systems. The last two columns in Exhibit 6 present the ACIR's general sales "tax capacity" and "tax effort" indexes for FY 1988. The tax capacity index measures the amount of sales tax revenue a state could produce if it applied a representative tax system composed of a nationally uniform rate and a standardized base. Variation in capacity across states results from differences in the value of taxable resources; therefore, tax capacity provides a means for assessing the available tax base. A tax capacity of 100 represents the national average; in 1988 Michigan recorded a 95 on the capacity index, suggesting that the state was slightly below average in terms of its available sales tax base.

The other ACIR index, tax effort, represents the ratio of actual tax collection to tax capacity. The effort index allows one to determine whether a state is underusing or overusing a particular revenue source relative to the national average of 100. Michigan ranked 41st among all states with a 76 on the sales tax effort index in 1988, suggesting Michigan's relative underutilization of the sales tax. The three states registering the highest tax effort marks—Washington, Hawaii, and New Mexico—also rank in the top four for per capita sales tax and sales tax as a percentage of personal income, and all tax most services.

The previous section characterized Michigan's sales tax base by comparing tax revenue and tax expenditures that result from exemptions. Exhibit 7 depicts the number of states taxing and exempting a variety of goods and services. In many areas there is widespread agreement on what to exclude from the tax base; only one state taxes materials used by manufacturers; two states tax prescription drugs (one taxes at a lower rate; the other offers a low-income credit); and three tax nonmedical professional services. Many states also agree on what items to tax; only three states exempt material used by contractors, and six exempt clothing. Yet in some areas—specifically food, consumer purchases of gas and electric, and repair charges—there is no consen-

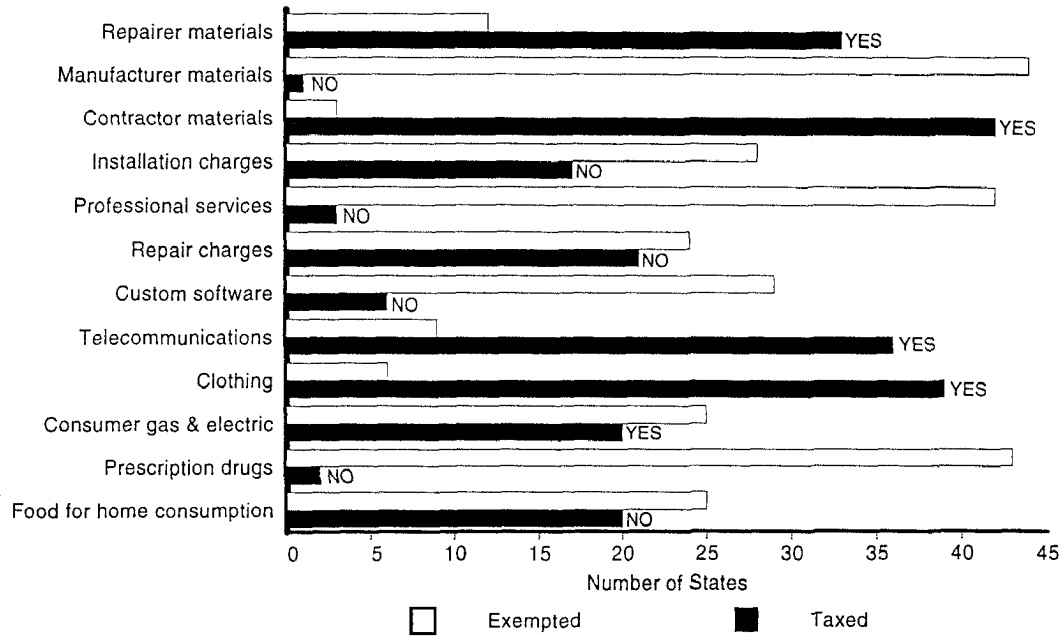
EXHIBIT 6: Interstate Comparisons of Sales Tax Measures, FY 1991

State	State Rate (FY 1993)	Maximum Combined State and Local (S+L) Rate	State General Sales Tax Revenue (in millions)	State Sales Tax as a Percent of Total State Taxes	S+L General Sales Tax Revenue (in millions)	Local as a Percent of State Revenue	Per Capita S+L Sales Tax Revenue	S+L Sales Tax as a Percent of Personal Income	Tax Capacity (U.S.=100; FY 1988)	Tax Effort (U.S.=100; FY 1988)
Alabama	4.000%	9.500%	\$1,050	26.6%	\$1,676	59.7%	\$410	2.76%	76	107
Alaska	No tax	4.000	No tax	0.0	77	NA	134	0.64	111	22
Arizona	5.000	7.200	2,006	42.6	2,443	21.8	651	4.14	104	128
Arkansas	4.500	5.500	877	37.1	1,034	18.0	436	3.10	77	108
California	5.500	7.750	14,340	32.0	17,984	25.4	592	2.90	110	103
Colorado	3.000	7.100	845	26.3	1,734	105.3	514	2.78	100	99
Connecticut	6.000	6.000	2,439	48.9	2,439	0.0	741	2.91	125	112
Delaware			No state or local general sales tax						112	1
Florida	6.000	7.000	8,139	59.1	8,235	1.2	620	3.41	118	108
Georgia	4.000	6.000	2,657	37.1	3,500	31.7	528	3.16	98	94
Hawaii	4.000	4.000	1,279	48.5	1,279	0.0	1,127	5.64	124	166
Idaho	5.000	5.000	404	33.5	404	0.0	389	2.62	74	101
Illinois	6.250	8.000	4,164	31.3	5,421	30.2	470	2.32	97	104
Indiana	5.000	5.000	2,538	41.1	2,538	0.0	452	2.71	92	105
Iowa	4.000	5.000	977	28.3	977	0.0	350	2.04	87	80
Kansas	4.900	6.250	918	32.8	1,132	23.2	454	2.51	87	104
Kentucky	6.000	6.000	1,300	25.8	1,300	0.0	350	2.35	89	78
Louisiana	4.000	9.000	1,308	30.4	2,678	104.7	630	4.37	85	141
Maine	5.000	5.000	497	31.9	497	0.0	403	2.35	112	83
Maryland	5.000	5.000	1,541	24.1	1,541	0.0	317	1.47	107	82
Massachusetts	5.000	5.000	1,909	19.7	1,909	0.0	318	1.41	123	65
Michigan	4.000	4.000	3,191	28.7	3,191	0.0	341	1.87	95	76
Minnesota	6.000	7.500	1,963	27.8	1,979	0.8	446	2.41	107	95
Mississippi	7.000	7.000	1,120	45.5	1,121	0.0	432	3.39	71	124
Missouri	4.225	6.475	1,863	37.3	2,536	36.1	492	2.83	94	105
Montana			No state or local general sales tax						84	1
Nebraska	5.000	6.500	624	35.3	723	15.9	452	2.61	91	82
Nevada	6.500	7.000	826	49.1	833	0.8	649	3.58	205	58
New Hampshire			No state or local general sales tax						142	11
New Jersey	6.000	6.000	4,043	34.7	4,043	0.0	521	2.10	118	78
New Mexico	5.000	5.875	939	45.0	1,141	21.5	737	5.26	82	170
North Carolina	4.000	6.000	1,690	21.5	2,491	47.4	370	2.30	93	90
North Dakota	5.000	6.000	235	31.2	251	6.8	396	2.60	97	75
Ohio	5.000	7.000	3,575	30.9	4,171	16.7	381	2.19	90	85
Oklahoma	4.500	7.500	964	24.9	1,525	58.3	480	3.14	86	108
Oregon			No state or local general sales tax						94	0
Pennsylvania	6.000	6.000	4,198	32.2	4,198	0.0	351	1.89	96	76
Rhode Island	7.000	7.000	448	35.7	448	0.0	447	2.37	104	85
South Carolina	5.000	5.000	1,438	36.5	1,438	0.0	404	2.71	86	99
South Dakota	4.000	6.000	248	47.0	337	35.9	480	3.07	87	127
Tennessee	5.500	7.750	2,363	54.8	3,101	31.2	626	4.00	88	146
Texas	6.250	8.250	8,295	51.8	10,094	21.7	582	3.54	95	121
Utah	5.000	6.250	740	39.7	900	21.6	508	3.72	78	123
Vermont	4.000	4.000	126	18.3	126	0.0	222	1.27	125	64
Virginia	3.500	4.500	1,559	22.8	2,051	31.6	326	1.68	107	66
Washington	6.500	8.200	4,758	59.6	5,439	14.3	1,084	5.90	95	206
West Virginia	6.000	6.000	817	35.1	817	0.0	454	3.32	83	87
Wisconsin	5.000	5.500	2,027	28.9	2,059	1.6	415	2.39	95	88
Wyoming	3.000	5.000	178	27.9	221	24.0	479	2.99	87	103

SOURCE: U.S. Bureau of the Census, *State Government Finances: 1991*, Series GF/91-3.

NOTE: Unless otherwise stated all comparisons are derived from FY 1991 data. Tax effort is nonzero for some states without a general sales tax because the index takes selective sales taxes into account.

EXHIBIT 7: Comparison of Tax Base Items



SOURCE: ACIR, *Significant Features of Fiscal Federalism*, 1992.

NOTE: "YES" signifies that the item is TAXED in Michigan; "NO" signifies that the item is NOT taxed in Michigan.

sus, but rather a nearly even split. Many of those states that do tax food offer a credit to low-income households. Compared to other states, Michigan maintains an average tax base, taxing or exempting with the majority of states in all but one category, consumer gas and electric.

CONCLUSIONS

As a component of the Michigan tax system, the state sales tax is underutilized. We base this conclusion on evidence from comparisons across states and comparisons against other Michigan taxes. This may be old news—Michigan’s sales tax has traditionally carried less than the 20 to 30 percent share of the state and local tax system that conventional policymakers prescribe; however, the recent landmark decision to cut school-based property taxes provides an excellent opportunity to end the historical practice of underusing the sales tax and overworking the property tax. (Incidentally, the same ACIR tax effort study that ranked Michigan 41st in

sales tax effort ranked the state 2d in property tax effort.)

Foremost in any plan to restore balance to the Michigan tax system should be the notion that tax changes should not make the system more regressive. Large increases in sales tax rates or broadening the tax base through cancellation of exemptions should be accompanied by a tax credit for low-income families. Hawaii, New Mexico, and South Dakota, three states with relatively broad tax bases, as well as four other states have successfully administered such sales tax-related credits.

Fortunately, Michigan has room to expand the sales tax. Our Great Lakes neighbors all currently levy higher sales tax rates, exert higher sales tax efforts, and place higher sales tax burdens on their consumers than we do; raising our rate or expanding our tax base would bring our sales tax system more in line with these states’ systems, just as the elimination of school millages will bring us more in line with those states’ property tax systems.

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