



“If there’s one certain way Michigan could lose its competitive standing, it would be to abandon its low, flat-rate income tax.”

Michigan’s tax competitiveness is at risk

26 states have cut income tax rates over the past five years

By Jared Walczak | March 2026

Michigan ranks 16th on the Tax Foundation’s State Tax Competitiveness Index. Ranking in the top third is fairly good, but Michigan’s trajectory is not. The state ranked 11th only five years ago and has been sliding ever since. While other states improve their tax competitiveness, Michigan is standing still.

Twenty-six states have cut income tax rates over the past five years, and 23 of those have cut their top rates. Michigan reduced income tax rates for 2023, but the 4.25% rate resumed the next year after the governor concluded that the revenue trigger that caused the rate cut should be only temporary.

While 18 states had top income tax rates below 5% in 2021, the numbers stands at 27 today, and 20 have rates below Michigan’s 4.25%.

Twenty years ago, only four states, including Michigan, had a single-rate income tax. Five years ago, there were seven. Today Michigan is one of fifteen states with a single-rate income tax.

Michigan’s low, single-rate income tax, along with a regionally competitive sales tax, is a major reason why it is in the top third of the State Tax Competitiveness Index. In last year’s ranking, however, Michigan tumbled from 14th to 19th overall on individual income taxes. The index, of course, is just a measure, and a rank is just a number. But that rank represents something real. Tax competition is ramping up, and states that rest on their laurels — or worse, surrender some of their competitive edge — risk slower economic growth and job creation.

Income taxes fall on labor and investment. High income tax rates cut into economic growth, and a strong and economically important impact will fall on small businesses. Higher rates will affect their propensity to invest, their ability to expand, and the number of people they employ.

Economic studies consistently show that high income tax rates are a drag on states’ economies. A Tax Foundation analysis estimated that a 9.25% top rate

in Michigan — as called for in the recently paused “Invest in MI Kids” campaign — would cost an estimated 43,000 jobs, cut wages by about 1%, and shrink the state’s economy by \$8.5 billion.

One of the virtues of a flat tax is that it keeps marginal rates in check. Economic decision-making takes place at the margin; the tax rate on the next dollar of income is the tax rate that matters most. When states must tax all income at the same rate, this exerts downward pressure on that rate. This is a major reason why Colorado’s income tax rate is 4.4%, Illinois’ is 4.95%, Pennsylvania’s is 3.07%, and Michigan’s is 4.25%, despite political pressures in each state that would likely yield much higher marginal rates if graduated-rate structures were permitted.

Michigan could take many steps to improve its tax climate. Immediate expensing of business machinery and equipment purchases would avoid penalizing capital investment, which current tax law does. Raising filing and withholding thresholds would ensure that nonresidents aren’t required to file and remit taxes to the state for visiting for a single day. Reforming the unemployment insurance tax regime could create greater stability, moving away from the current system, under which tax burdens increase dramatically during an economic downturn, when businesses struggle to avoid further layoffs.

But if there’s one certain way Michigan could lose its competitive standing, it would be to abandon its low, flat-rate income tax.

And as more states enhance their tax competitiveness, the list of options expands, making it easier to live, work, invest, or locate one’s business in a low-tax

state. For all their advantages, Florida and Texas aren’t for everyone. But with a growing number of states offering a competitive tax environment, the prospects of a good fit increase dramatically, and the costs of states disregarding tax competitiveness rise accordingly.

Michigan and its regional peers face stiff economic headwinds, while other states, particularly in the Sunbelt and the Mountain West, experience robust economic and population growth. Lawmakers in Lansing can’t control every factor contributing to these dynamics. But they can shape the state’s tax code in ways that will either attract residents and spur economic growth, or turn away both. They’ve received a reprieve, for now, from the effort to make things worse. It’s time for them to act.

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