

# Overview of the Michigan Business Tax

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FTA Revenue Estimation and  
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Portland, Maine  
September 2008

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## Michigan's Single Business Tax (SBT)

- Enacted in 1975, effective 1/1/76
- Replaced Michigan's corporate income tax and six other business taxes
- Modified value added tax
- Initially based on "benefits-received" principle rather than an "ability to pay" principle
- Tax calculation used an additive VAT calculation method – starts with business income and adds back labor and capital inputs

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## Taxes SBT Replaced

- Corporate Income (39.0% of total)
- Financial Institution Income (2.3% of total)
- Corporate Franchise (20.8% of total)
- Business Intangibles (3.8% of total)
- Local Property Tax On Inventory (33.4% of total)
- Other (0.8% of total)

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## SBT Repeal

- In 1999, rate cuts enacted to drop rate by 0.1 percentage points per year until rate was zero (23 years), but cuts stop if BSF < \$250M
- BSF falls below \$250M in 2002, rate cuts stop
- In 2002, legislation enacted to repeal SBT in Dec 2009
- In the summer of 2006, legislature enacted voter initiated repeal effective December 31, 2007
- In FY 07, SBT equaled 7.3% of state taxes and 19.5% of unrestricted revenues
- MBT enacted in July of 2007 to start in January of 2008.

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## Why was the SBT Repealed

- Additive method of VAT led to negative perceptions – taxpayers used to subtracting from base, not adding to it
- Firms did not like having to pay in years they lost money
- Michigan's economy was uniquely bad this decade and business tax was unique – causality was assumed
- Comparing SBT simply to other states' corporate income taxes gave the false impression that business taxes were high in Michigan

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## Michigan Business Tax

- New tax base of income and gross receipts less purchases shifts part of burden to **ability to pay** (i.e. income) while maintaining a stable base
- Substantial **personal property tax relief** addresses a major business concern
- Tax credits provide incentives **to invest** in Michigan, **to employ** Michigan residents, and **to perform research and development** in the state
- Special provisions **lower tax burden** for small businesses helping them to grow
- SBT revenues **fully** replaced

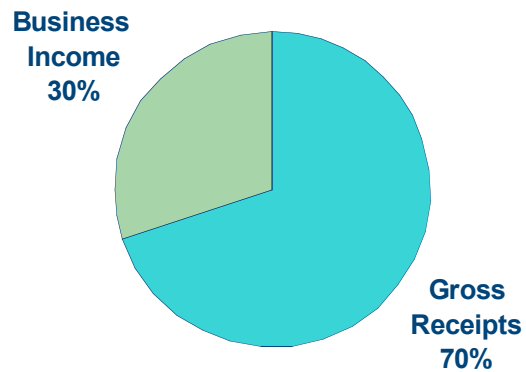
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## New Tax Base

- General Tax Base
  - Modified Gross Receipts taxed at 0.8%
  - Business Income taxed at 4.95%
- Insurance Companies
  - 1.25% tax on direct premiums
- Financial Institutions
  - 0.235% franchise tax on net capital

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## MBT Tax Base



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## Apportionment

- Single factor apportionment based on sales (MI sales/sales everywhere)
- No throwback sales
- Sales are sourced to another state if that state has jurisdiction to tax even if that state does not do so

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## Business Income Tax Base

- Starting point is federal taxable income from business activity
- Includes non-corporate entities
- Unitary groups
  - File a combined return
  - Add tax bases of group members – apply combined apportionment %
  - Foreign operating entities, insurance companies, & financial institutions cannot participate
- Beginning in 2008, business loss may be carried forward 10 years

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## Modified Gross Receipts Base

- Tax base is a taxpayer's gross receipts less "purchases from other firms" before apportionment
- Purchases from other firms means
  - Inventory acquired during the year
  - Depreciable assets acquired during the year
  - Materials and supplies, including repair, parts and fuel

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## Insurance Company Tax

- In lieu of modified gross receipts and business income taxes
- 1.25% of gross direct premiums written on property or risk located in Michigan
- No apportionment – only premiums on Michigan risks and property are taxed
- Retaliatory tax as described in insurance code is still in place (same as SBT provision)

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## Financial Institution Tax

- Financial institution tax limited to
  - Banks, thrift banks, and savings and loans
  - Entity owned directly or indirectly by a financial institution
  - A unitary business group of these entities
- Net capital defined as:
  - The average of net capital for current tax year and 4 prior years (computed per GAAP)
  - Exception for new businesses

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## Personal Property Tax Relief

- Commercial personal property exempt from 12 of 24 education mills (average 23 percent cut)
- Industrial property exempt from 24 education mills and firms receive 35 percent refundable credit for remaining industrial personal property tax
- Provides a personal property tax cut of 65 percent on average for industrial property
- Schools protected by dedicating a portion of the MBT to the School Aid Fund
- No cuts to city, village, townships, and county property taxes
- Reduces burden on mobile capital

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## Special Provisions for Small Businesses

- Firms with less than \$350,000 in gross receipts exempt
- Full tax liability phased-in for \$350,000 to \$700,000 in gross receipts through a credit
- Allow qualifying firms to pay 1.8% on adjusted business income
- Raise alternate tax officer compensation disqualifier phase-out to \$160,000 to \$180,000
- Double gross receipts phase-out to \$19-20 million
- Entrepreneurial credit to encourage hiring and investment in Michigan

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## Credits Provide Incentives to Do Business in Michigan

- **Compensation credit** – for 0.37 percent of Michigan compensation
- **Investment tax credit** -- for 2.9 percent of Michigan investment
- **R&D Credit** – for 1.9 percent of Michigan research and development expenses
- Sum of compensation and investment credit cannot exceed 52 percent of MBT liability
- Sum of all 3 credits cannot exceed 65 percent of liability
- Credit provisions reduced for 2008

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## Transition Provisions

- Unused SBT credit carry-forwards may be claimed on 2008 and 2009 MBT returns
- SBT Brownfield and Historic Preservation credits may be carried forward for 10 years after claim
- 65% of any SBT business loss incurred in 2006 or 2007 may be deducted against 2008 modified gross receipts base

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## MBT Surcharge

- PA 145 of 2007 repealed service tax and replaced revenue with an MBT surcharge
- Surcharge is 21.99% of tax before credits
- Major credits are lowered
- Due to timing, changes are an approximately \$100 million tax cut in FY 08, revenue neutral with respect to replacing service tax thereafter
- For financial institutions, surcharge is 27.7% for 2008 and 23.4% thereafter
- No surcharge on insurance company tax
- Surcharge expires in 2017

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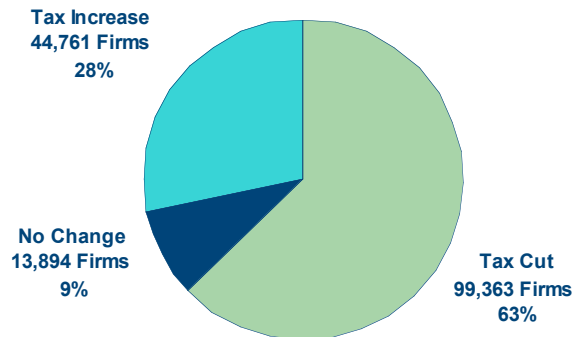
## MBT Changes to Credit Provisions

In addition to the 21.99% surcharge, the following changes were made to the MBT credit provisions

MBT Provision	Original	After PA 145	
		2008	2009
Compensation Credit	0.370%	0.296%	0.370%
Investment Tax Credit	0.290%	0.232%	0.290%
Research & Dev. Credit	1.900%	1.520%	1.900%
Max of Comp and ITC Credits	65.0%	50.0%	52.0%
Max of Comp, ITC, R&D Credits	75.0%	65.0%	65.0%

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## Two Out Of Three Taxpayers Pay The Same Or Less Under The MBT



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Note: Estimates based on TY 2009 law using 2003 SBT data.

## Who Will Pay Less

- Manufacturing firms
- Small businesses between \$10 and \$20 million of gross receipts
- Small businesses under \$10 million with income to owners over \$115,000
- Michigan multi-state firms

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## Who Will Pay More

- FIRE
- Profitable firms
- Firms without much personal property
- Firms that operate in Michigan but have little payroll or property here

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## MBT Revenue Trigger

- MBT has a trigger to ensure that it does not represent a large tax increase
- If revenues exceed trigger, 60% of excess refunded to taxpayers and 40% deposited into BSF
- Triggers if revenues grow faster than inflation plus  $\frac{3}{4}\%$

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## Treasury Resources Available

- Department web page has resources for taxpayers
  - MBT estimator
  - FAQs posted to explain various aspects of MBT (questions can be submitted)
  - Presentations and Webinars provide additional detail on tax
- Information can be found at:  
[www.michigan.gov/treasury](http://www.michigan.gov/treasury)

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