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BILL ANALYSIS

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Senate Bill 1 (as introduced 1-19-11)
Sponsor: Senator Dave Hilbenbrand
Committee: Finance

Date Completed: 1-28-11

CONTENT

The bill proposes to repeal the Michigan Business Tax Act.

MCL 208.1101-208.1601

BACKGROUND

Public Act 36 of 2007 enacted the Michigan Business Tax Act to replace the former Single Business Tax Act. The Michigan Business Tax (MBT) generally is levied on any person or entity conducting business activity in Michigan. For most types of businesses, the MBT has two components: 1) the business income tax, and 2) the modified gross receipts tax. Separate taxes apply to insurance companies and financial institutions, in lieu of the business income tax and modified gross receipts tax. The Act also imposes a surcharge on businesses' MBT liability; the surcharge does not apply to insurers, or to financial institutions that exercise only trust powers.

In addition, the Act provides for a number of credits against tax liability.

MBT Liability

The business income tax is imposed at the rate of 4.95% of the business income tax base, which is Federal taxable income derived from business activity, subject to various adjustments and apportionment. The modified gross receipts tax applies to taxpayers with "substantial nexus" in Michigan. The tax is imposed at a rate of 0.8% of gross receipts, which include all amounts a taxpayer receives from intrastate, interstate, and foreign commerce, less purchases from other firms (e.g., inventory and capital expenditures). Both the business income tax and the modified gross receipts tax are apportioned to Michigan based on a sales factor (total sales in Michigan divided by total sales everywhere).

The tax on insurance companies is 1.25% of gross direct premiums on property or risk in Michigan. Financial institutions are subject to a franchise tax on the value of their net capital stock. The rate of this tax is 0.235%.

The surcharge is applied to the liability generated by a business's income tax and gross receipts, after apportionment and before the application of credits. The rate of the surcharge is 21.99% (or 23.4% for nonexempt financial institutions). The maximum amount of the surcharge is $6.0 million per taxpayer.

MBT Credits

The MBT Act provides for a number of credits, including some that were carried over from the Single Business Tax (SBT) Act. Credits new to the MBT include the following:

-- Compensation credit: 0.37% of a taxpayer's compensation paid in this State.
-- Investment credit: 2.9% of the cost of new capital assets located and used in the State.
-- Personal property tax credit: 35.0% of property taxes paid on industrial personal property, 13.0% paid on eligible telephone personal property, and 10.0% paid on eligible natural gas pipeline property.
-- Research and development (R&D) credit: 1.9% of a taxpayer's qualified R&D expenditures in Michigan (plus a second credit for R&D and technology innovation, available for 2008, 2009, and 2010, subject to approval by the Michigan Economic Growth Authority).
-- Entrepreneurial credit: 100% of MBT liability attributable to increased employment, for a nonretail establishment meeting gross receipts, new jobs, and capital investment criteria, for tax years 2008, 2009, and 2010.

In addition, the gross receipts filing threshold credit essentially phases in MBT liability for businesses with gross receipts of more than $350,000 (the filing threshold) but less than $700,000.

Credits new to the MBT also are available for specific taxpayers or types of businesses. These include the motor sports entertainment complex credit; the sports and entertainment facility credit; the motor vehicle dealer inventory credit; a credit for charitable contributions in excess of $50,000 to certain cultural institutions; and compensation-based credits for two specific Michigan-headquartered food retailers.

In addition, the MBT Act contains various credits that were created after Public Act 36 of 2007 was enacted. These include the film credits that are available for production expenditures, job training costs, and investments in production facilities; several credits related to advanced battery technology; and an "anchor company" credit, based on qualified new jobs created by suppliers and customers of a qualified high-technology business.

Credits under the MBT Act that were carried over from the SBT Act include the following, among others:

-- Renaissance zone credit.
-- Brownfield credit.
-- Historic rehabilitation credit.
-- A credit for qualified start-up businesses.
-- A credit for investors in an "early stage venture".
-- A credit for worker's disability compensation payments made by an employer.
-- A credit for taxpayers certified under the Michigan Next Energy Authority Act.
-- A credit for charitable contributions to certain public institutions.
-- A credit for contributions to the endowment fund of a community foundation or an education foundation.

The MBT Act also allows a small business credit for taxpayers with maximum gross receipts of $20.0 million, maximum business income of $1.3 million, and maximum single officer's or shareholder's compensation or individual or pass-through entity owner's distributive income share of $180,000. (The SBT Act contained this credit subject to lower caps.) The small business credit can effectively reduce a taxpayer's MBT liability to 1.8% of its adjusted business income.

In addition, credits carried over from the SBT Act include a credit for authorized businesses based on payroll and health care benefits attributable to new or retained jobs, under agreements with the Michigan Economic Growth Authority.

While some of the MBT credits are nonrefundable, others are refundable, which means that the taxpayer will receive a payment from the State if the amount of the credit exceeds the business's tax liability. (Examples of refundable credits are the R&D credit and the film production credit.) In other cases, credits that exceed liability may be carried forward to subsequent tax years. Also, some credits are assignable, which allows a taxpayer receiving the credit to sell it to another taxpayer that can use it. (An example of an assignable credit is the historic preservation credit.)

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would reduce General Fund and School Aid Fund revenue. Assuming the bill were adopted before September 30, 2011, the reduction in FY 2010-11 would depend on when the bill was enacted, if it were given immediate effect, and whether it was made retroactive. Net revenue from the MBT is estimated to generate approximately $2.1 billion during FY 2010-11, and $2.2 billion during FY 2011-12, including $739.2 million and $750.2 million in School Aid Fund revenue during the two fiscal years, respectively.

Because the bill would not affect tax payments or refund requests for prior tax years, State revenue would still be affected by late payments and refund requests even after the MBT Act was repealed. Based on the revenue history after the Single Business Tax Act was repealed, the net impact of these prior tax year issues would be negative, meaning that the total impact of the bill would be not only the loss of $2.2 billion in net revenue during FY 2011-12, but an additional loss of revenue attributable to refunds for prior tax years.

The MBT Act also contains a number of provisions, particularly tax credits, designed to offset or subsidize certain costs (such as personal property taxes on industrial personal property, motion picture production costs, and crowd control costs at a motor sports entertainment complex) and/or to fulfill agreements reached with the Michigan Economic Growth Authority (MEGA credits, brownfield credits, battery credits, etc.). To the extent the State chose or was required to continue the essence of these provisions through other types of credits and/or direct expenditures, State revenue would fall by more than the reduction in MBT revenue or expenditures would increase, or both would occur.

It appears that the bill also would eliminate credits claimed under the MBT through provisions in the Natural Resources and Environmental Protection Act for farmland preservation activities.

Fiscal Analyst: David Zin