



**Senate Fiscal Agency**  
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BILL



ANALYSIS

**Telephone: (517) 373-5383**  
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House Bill 5100 (as reported without amendment)  
Sponsor: Representative Ken Sikkema  
House Committee: Commerce Senate  
Committee: Financial Services

Date Completed: 2-12-96

### **RATIONALE**

The Business Corporation Act allows a corporation to lend money to, guarantee an obligation of, or otherwise assist an officer or employee of the firm or its subsidiary if the corporate board determines that doing so could reasonably be expected to benefit the firm. In recent years, more publicly held corporations reportedly have offered their employees loans to purchase shares in the company as a means to motivate them to help improve the company's performance. Since the Business Corporation Act does not specify a maximum rate of interest, loans made by a corporation to its officers or employees cannot exceed 7% annually, the maximum interest rate otherwise allowed under the general usury Act (MCL 438.31).

This presents an occasional problem for companies and their employees due to a rule established by the Internal Revenue Service (IRS) regarding the threshold at which an employee benefit is considered taxable. On a monthly basis, the IRS determines what is known as the applicable Federal rate (AFR) for long-term loans, which designates the *lowest* interest rate that may be charged without imputing income to the borrower. When the AFR, which is closely tied to the prime rate, is set at a rate above 7%, as it has been in recent months, loans issued by companies to their employees are considered taxable income to the employees. Some people believe that, to prevent employer-to-employee loans from being considered a taxable benefit, the Business Corporation Act should specifically allow interest on these loans to be assessed at any rate up to the criminal usury rate, which is 25%.

### **CONTENT**

The bill would amend the Business Corporation Act to specify that a loan issued by a corporation to an officer or employee of the corporation or one of its subsidiaries, for the officer or employee to purchase shares of the corporation or a subsidiary, could be made at any rate of interest not exceeding the rate allowed under Public Act 259 of 1968. (That Act provides that a person is guilty of criminal usury when he or she knowingly charges, takes, or receives interest at a rate exceeding 25% annually.)

MCL 450.1548

### **ARGUMENTS**

*(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)*

#### **Supporting Argument**

The bill would make it possible for a corporation regulated under the Business Corporation Act to lend money to an officer or employee of the company for him or her to purchase shares of the company without the loan's being subject to Federal income taxes as a taxable benefit. This type of benefit apparently has become more common among companies, in order to encourage employees to feel as if they have more of a stake in the company's performance. Since these loans currently cannot be made at a rate exceeding 7% interest, however, they may be considered taxable income by the IRS if the applicable Federal rate, which is calculated monthly, exceeds 7%, as it has at times over the last year or so. By raising to 25%

the cap on the rate that may be charged on employees' loans, the bill not only would give companies the ability to make these loans at a rate above the AFR, so they could be excluded from Federal income taxes, but also would give employers some flexibility in providing the loans if interest rates rose in the future.

Legislative Analyst: P. Affholter

#### **FISCAL IMPACT**

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: M. Barsch

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.