

Michigan is Getting Closer to a Replacement Tax

May 4, 2007

Last week, House Speaker Andy Dillon (D-Redford) introduced the House Democrats' replacement tax plan (HB 4367), which was introduced as a substitute to the Governor's previously introduced Michigan Business Tax (MBT).

The House passed HB 4367 on May 2, and the bill is expected to be sent to the Senate soon. The Senate also passed its business tax proposal, SB's 94, 95 and 96, Thursday. It is expected that the chambers will soon be meeting to discuss how to develop a final plan.

The new MBT would levy both a net income tax and a net worth tax. The net income tax would generally follow federal taxable income, and would have some protections of PL 86-272. The net worth tax would be imposed on a broader basis, and would be imposed on total assets less total liabilities, with only water's edge nexus protections. Both levies would be apportioned based on sales to Michigan.

Other highlights of the bills include:

- Net income tax rate of 6.95%

- Net worth tax rate of .488%

- Market sourcing for sales of services and intangible property

- Required unitary combination filing--using a 50% common ownership level with an elimination of intercompany transactions

- 46% reduction in personal property tax for industrial and commercial property

- Allowance for SBT credit carryforwards and loss deductions

It is important to note that HB 4386, the nexus bill which attempts to codify affiliate nexus on an extremely broad basis, was also passed by the House on April 17 on a bi-partisan basis, and was received by the Senate the following day. The intent of the legislature is to impose the net worth tax (as well as all other taxes administered under Michigan's Revenue Act) to the fullest extent allowed by the U.S. Constitution.

The new MBT provides significant tax relief in the form of credits for in-state compensation paid, in-state investment and in-state R&D expenses, which can be applied to reduce the MBT liability up to 75% of the tax due. There is some concern that some of the credits and refunds may be suspect under several constitutional provisions.

The new MBT has been endorsed by the Michigan Chamber, which had previously supported its own proposal (a mix of a net income tax and gross receipts tax). Further support is expected, and the House Plan may quickly gather significant momentum to provide the State with an agreed-to replacement to the Single Business Tax. This relief comes just on the heels of further downgrades to the State's credit rating by Fitch and Moody.

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However, a budget deficit still remains for the current fiscal year, which will be unaffected by the new MBT, which will not be effective until 1/1/08. Additional revenue raisers still under consideration by the Legislature include an increase in the personal income tax rates (effective retroactively to 1/1/07), a modified version of the two-cent excise tax on services, or an increase in the current sales tax rate on tangible personal property. There is some discussion that the choice may be put to voters to select one, as the Michigan Constitution requires public approval of any new or increased rates.

If you have any questions regarding this alert, please contact any of the SALT tax experts:

Samuel J. McKim III, Robert F. Rhoades, Joanne B. Faycurry, or Jackie J. Cook.