Quarterly Financial Statement Releases May Reveal Significance of Lack of FAS 109 Relief in Michigan Corporate Income Tax

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When Michigan Governor Rick Snyder signed Michigan's new corporate income tax into law on May 25, one provision not contained in the new law was a relief mechanism from the adverse financial statement impact the new tax may have on some companies, despite the fact that the MBT, which the new tax replaces, contained such a provision. Other states that have made substantial changes in their tax structures in recent years including Ohio, Texas, and Massachusetts, adopted mechanisms providing relief from the financial statement impacts of their tax changes.

The so-called "FAS 109 fix" in the MBT created a deduction that allowed taxpayers to recognize a deferred tax asset for financial statement purposes. The deduction would have been available to companies in years 2015-2029, with most of the benefits in the later years. The deduction was designed to offset the adverse financial statement impact that would have otherwise been recorded when the MBT was enacted in 2007. Under the accounting standard known as FAS 109, the adverse financial statement impact arose because the MBT implemented an income tax and many companies had to account for "deferred income taxes" at the new MBT rates which required them to take large financial statement charges in the quarter of enactment for the cumulative effect of the new MBT rates. With the repeal of the MBT, that deduction goes away before it was ever available. The new corporate income tax creates deferred tax financial statement impacts similar to those the MBT had created. The result is that companies will need to record the financial statement impact of the new corporate tax in the period of enactment, which for calendar year taxpayers is the quarter ended June 30, 2011.

Corporations with substantial capital investments in Michigan sought a FAS 109 relief mechanism similar to the one enacted in the MBT and argued relief was needed in order to avoid a detrimental impact of what was designed to be a very pro-business change in the Michigan tax structure, but were unsuccessful in that effort. It is not clear whether the lack of support for the provision was due to the potential revenue impact, skepticism regarding the size or consequence of the financial statement charge, or the perception of the provision as a form of "loophole."

In addition to the deferred tax liability financial statement impact of the new corporate tax, some negative financial statement impacts may also be recognized because the corporate income tax does not allow a deduction for net operating losses incurred in the years 2008-2011 while the MBT was in effect. The lack of a net operating loss carry forward from the MBT years to the corporate income tax would require companies that had such MBT loss carry forward on their books as a deferred asset as required under FAS 109 to write those assets off, resulting in further financial statement charges to those companies.

Financial statement disclosures by public companies for the quarter the new tax was enacted may reveal the magnitude of the financial statement impact of the absence of a FAS 109 relief mechanism in the new corporate tax. This could in turn motivate companies with substantial negative impacts to push for a fix by year end to reverse those mid-year charges. Whether they can persuade the legislature and Governor to support such a provision is another question.

If you have questions, please contact a Miller Canfield State and Local Tax attorney or the authors:

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