

## **The New Michigan Business Tax Analysis for Family Businesses**

The New Michigan Business Tax will affect every business operating in Michigan. It is important to examine your business structure before the end of this year to take appropriate planning steps to minimize tax liability and avoid compliance pitfalls.

The new Michigan Business Tax package replaces the Single Business Tax with two basic, broadly applicable taxes: 1) a modified gross receipts tax and 2) a business income tax. The gross receipts tax rate is 0.8% which is applied to all gross receipts minus purchases from other firms. The business income tax is imposed at a rate of 4.95% on federal adjusted business income (with adjustments).

### **Impact on Family Businesses**

The Department of Treasury is asserting that the modified gross receipts tax applies to capital gain of individuals, trusts, estates and partnerships even if the person is not engaged in a trade or business. This greatly expands the reach of the tax and has potential for double taxation.

### **Tax Bases**

The business income tax will be imposed at 4.95% on federal taxable income with some modifications. The modified gross receipts tax is imposed on gross receipts less purchases from other firms at a rate of 0.8%. Certain exceptions from the gross receipts tax base for amounts received in an agency capacity and a limitation to inclusion of only net gain on certain capital investments will benefit family businesses.

### **Apportionment**

Michigan-based businesses that sell outside the state will benefit from the shift to a 100% sales factor to apportion tax base among states. The move away from using a factor that includes property or payroll increases the liability on businesses that use Michigan's markets, but have little presence here otherwise. Family businesses may benefit from the move to a market-based sourcing for sales of services and intangibles. Sales of services and intangible property are sourced to Michigan if the customer receives the benefit of the services or intangibles in the state. Sales of tangible personal property continue to be sourced to Michigan when property is received in Michigan.

### **New Mandatory Unitary Filing**

The new tax requires firms to file on a "unitary" basis. This means that the taxpayer no longer has the option of filing a consolidated return, or on a stand-alone basis, if certain requirements are met. If a business has nexus in Michigan, the filing must include all entities that are included in that business's unitary group, with the exception of certain defined non-U.S. persons.

### **Minimum Tax – Small Business Exception**

Taxpayers with apportioned gross receipts under \$350,000 will not be subject to tax. The tax is phased in from \$350,000 to \$700,000 in receipts to eliminate any cliff effect. Taxpayers that have less than \$20 million in apportioned gross receipts and meet certain compensation and income distribution limitations are eligible to be taxed at 1.8% on modified federal taxable income. The "unincorporated" credit under the Single Business tax has been discontinued.

### **Credits**

Beginning in 2008, rates for industrial and commercial personal property will be reduced by 12 and 24 mills respectively in most areas and a 35% refundable MBT credit may be applied to the remaining industrial personal property tax liability. These reductions also apply on a pro rata basis for property that is currently under industrial property tax abatements. In addition, firms will continue to benefit from an

investment tax credit (ITC) for property placed in Michigan (2.9% of net investment), as well as a credit for research and development expenditures in Michigan (1.9% of R&D expenditures). However, a taxpayer may not claim both credits for the same expenditure. In addition, a credit equal to 0.37% of compensation paid is available. The combined ITC and compensation credit may not exceed 65% of the taxpayer's liability.

## **Tax Incentives**

Key tax incentives such as the MEGA employment credit will still be available to manufacturers that are expanding, relocating or retaining jobs in Michigan. Existing MEGA deals entered into under the Single Business Tax will continue, but will also be subject to recapture provisions if jobs are moved out of state.

## **Potential Tax Rebate**

If net cash revenues collected under the SBT and MBT exceed estimates for revenue neutrality by 5% or more for 2008 and 2009, the revenues in excess of \$5 million will be rebated pro rata to net cash taxpayers.

## **Honigman's MBT Services**

As you analyze the impact of the new Michigan Business Tax on your business, Honigman can assist by providing the following critical services:

- Estimate of tax liability under different scenarios using Honigman's MBT Tax Calculator
- Analysis of applicability of MBT to business and personal investment activities
- Identification of strategies to minimize impact of MBT on investment activities
- Analysis of apportionment positions applicable to business and investment activities
- Analysis of components of tax bases, especially gross receipt tax base
- Identification of strategies to reduce tax base and expand deductions
- Analysis of unitary filing group and identification of strategies to reorganize tax filings to minimize taxes
- Evaluation of steps to take to ensure qualification for any tax rebate
- Updates on technical corrections and interpretations

### **For more information, please contact:**

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