

Understanding the New Michigan Business Tax

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 Businesses

The new Michigan tax regime is revenue neutral for all businesses but will change the distribution of the tax base away from manufacturing companies, with any increases borne by non-manufacturing companies. According to the Department of Treasury, firms doing business in Michigan only and multi-state firms located outside of Michigan will experience a tax increase as a group, while Michigan-based, multi-state businesses will experience a reduction.

Key Provisions

One of the key components of the plan that benefits Michigan companies is the combined rate reduction and Michigan specific credits. Businesses can continue to claim the 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 new 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.

In addition, some firms will benefit from refundable credit for industrial personal property taxes. Beginning in 2008, rates for industrial personal property will be reduced by 24 mills 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. Tax rates for commercial personal property will be reduced by 12 mills in most areas.

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. Sales of tangible personal property are sourced to Michigan if the property is received in Michigan. Sales of services and intangible property are sourced to Michigan if the customer receives the benefit of the services or intangibles in the state.

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' unitary group, with the exception of foreign operating entities.

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.

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 components of tax bases, especially gross receipts
- Identification of strategies to reduce gross receipts and expand deductions for purchases from other firms
- Assistance in maximizing property tax credits
- Identification of new credits and incentives available to your business
- Analysis of unitary filing group and identification of strategies to reorganize tax filings to minimize taxes
- Assistance with key tax classification issues
- Evaluation of steps to take to ensure qualification for any tax rebate
- Updates on technical corrections and interpretations

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