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Senate Bill 1500 (as enrolled)
Sponsor: Senator Bill Bullard, Jr.
Senate Committee: Finance
House Committee: Tax Policy

PUBLIC ACT 622 of 2002

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RATIONALE

The Michigan Renaissance Zone Act provides for the designation of renaissance zones in which businesses and residents receive certain tax exemptions and credits. Various tax statutes prescribe the specific tax exemptions and/or credits that may be claimed. Regarding business taxes, the Single Business Tax (SBT) Act provides a credit for general business activity conducted within a renaissance zone. Public Act 531 of 2002 amended the SBT Act to allow another credit for certain qualified business activity. Under the SBT Act, "qualified business activity" means research, development, or manufacturing of an alternative energy system, vehicle, or technology, an alternative energy marine propulsion system, or renewable fuel, as those terms are defined in the Michigan Next Energy Authority Act. The credits for business activity conducted in a renaissance zone and for qualified business activity are determined by similar calculations prescribed in the SBT Act, using specific formulas that attempt to measure a business's activity within and outside a renaissance zone compared with the business's total activity in the State; thus, the calculations aim to limit the credits to actual activity within a zone.

Reportedly, some businesses have placed storefront offices in renaissance zones, and then attempted to claim the credit for business activity that actually occurred outside the zones. It was suggested that the calculation of the credits be changed to prevent such claims.

CONTENT

The bill amended the Single Business Tax Act to revise the calculation of the credit allowed for a business located and conducting business activity within a renaissance zone, and the calculation of

the credit allowed for an eligible taxpayer that has qualified business activity, for tax years beginning after December 31, 2002. A taxpayer conducting business activity in a renaissance zone may claim either the amount calculated under the existing formula, or an amount based on "adjusted services performed in a designated renaissance zone". An eligible taxpayer may claim either an amount based on the existing formula (as modified by the bill) or an amount based on "adjusted qualified business activity performed in this state outside of a renaissance zone", whichever is less.

Business Activity in Renaissance Zone

Under the Act, for a business located in and conducting business activity in a designated renaissance zone, the credit is equal to the amount of the taxpayer's "tax liability attributable to business activity conducted within a renaissance zone". The bill retains the formula for determining "tax liability attributable to business activity conducted within a renaissance zone" but refers to the formula as the "renaissance zone business activity factor" (defined below). For tax years beginning on or after January 1, 2003, the bill allows a taxpayer to claim either that amount or either of the amounts described below:

A business that first locates and begins conducting business activity in a renaissance zone after November 30, 2002, may claim the lesser of the following:

- The tax liability attributable to business activity conducted in a renaissance zone in the tax year.
- 10% of adjusted services performed in a designated renaissance zone.

A business that is located and conducting business activity within a renaissance zone before December 1, 2002, or a business that before December 1, 2002, entered into a purchase or lease agreement for real or personal property to be used for business activity within a renaissance zone, may claim the greater of the following:

- The lesser of the amounts calculated above.
- The lesser of the following: 1) the tax liability attributable to business activity conducted within a renaissance zone in the tax year, or 2) the credit allowed for the tax year beginning in 2002 plus 2% of the increase in the amount of "adjusted services performed in a designated renaissance zone" (applicable to a taxpayer other than a partnership, limited liability company, S corporation, or individual) for the tax year over the amount calculated for such services for the tax year beginning in 2002.

The bill defines "adjusted services performed in a designated renaissance zone" as either of the following:

- The sum of the taxpayer's payroll for services performed in a designated renaissance zone plus the amount equal to the amount added pursuant to Section 9(4)(c) for the tax year for renaissance zone property exempt under the General Property Tax Act, in the tax year or, for new property, in the immediately following tax year. (Section 9(4)(c) of the SBT Act requires a taxpayer, in determining its tax base, to add the amount of a deduction, amortization, or write-off related to the cost of tangible assets, to the extent deducted in arriving at Federal taxable income.)
- For a partnership, limited liability company, S corporation, or individual, the amount determined above plus the product of the following as related to the taxpayer, if greater than zero: business income; the apportionment factor as determined under Chapter 3 of the SBT Act; and the "renaissance zone business activity factor".

"Renaissance zone business activity factor" means a fraction, the numerator of which is the ratio of the average value of the taxpayer's property located in a designated renaissance zone to the average value of the

taxpayer's property in this State plus the ratio of the taxpayer's payroll for services performed in a designated renaissance zone to all of the taxpayer's payroll in this State and the denominator of which is two.

Qualified Business Activity

Previously, for tax years beginning after 2002, the Act allowed an eligible taxpayer (a taxpayer that has proof of certification of qualified business activity under the Michigan Next Energy Authority Act) to claim a credit for a tax year equal to the amount by which the taxpayer's tax liability attributable to qualified business activity for the tax year exceeded the taxpayer's "baseline tax liability attributable to qualified business activity". Under the bill, an eligible taxpayer may claim the lesser of that amount or 10% of the amount by which the taxpayer's "adjusted qualified business activity performed in this state outside of a renaissance zone" for a tax year exceeds such activity for the 2001 tax year. (Under the SBT Act, "qualified business activity" means research, development, or manufacturing of an alternative energy marine propulsion system, an alternative energy system, an alternative energy vehicle, alternative energy technology, or renewable fuel.)

The bill defines "adjusted qualified business activity performed in this state outside of a renaissance zone" as either of the following:

- The taxpayer's payroll for qualified business activity performed in this State outside of a renaissance zone.
- For a partnership, limited liability company, S corporation, or individual, the amount calculated above plus the product of the following as related to the taxpayer: business income; the apportionment factor as determined under Chapter 3; and the "alternative energy business activity factor".

"Alternative energy business activity factor" means a fraction, the numerator of which is the ratio of the value of the taxpayer's property used for qualified business activity and located in this State outside of a renaissance zone for the year for which the factor is being calculated, to the value of all of the taxpayer's property located in this State for that year plus the ratio of the taxpayer's payroll for qualified business activity

performed in this State outside of a renaissance zone for that year to all of the taxpayer's payroll in this State for that year, and the denominator of which is two.

Previously, "baseline tax liability attributable to qualified business activity" meant the taxpayer's tax liability for the 2001 tax year 1) multiplied by a) the ratio of the value of the taxpayer's property used for qualified business activity and located in this State outside of a renaissance zone for the 2001 tax year, to the value of all of the taxpayer's property in this State for that tax year, plus b) the ratio of the taxpayer's payroll for qualified business activity performed outside of a renaissance zone for the 2001 tax year to all of the taxpayer's payroll for that tax year in this State; and 2) divided by two. Under the bill, "baseline tax liability attributable to qualified business activity" means the taxpayer's tax liability for the 2001 tax year multiplied by the taxpayer's alternative energy business activity factor for the 2001 tax year.

MCL 208.39b & 208.39e

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

Renaissance zones were created as a tool to revitalize certain areas by helping to generate and/or increase economic activity. Some communities, both urban and rural, face multiple challenges to economic development, such as deteriorated infrastructures and abandoned residential and commercial sites. To create incentives to invest, build, and live in these areas, the law provides for the designation of a limited number of renaissance zones, in which businesses and individuals may claim certain tax exemptions and credits.

The SBT Act provides a credit against the tax for taxpayers that conduct business activity within a renaissance zone. To determine the value of this credit, the Act prescribes calculations that attempt to separate a taxpayer's business activity in a zone, which is eligible for the credit, from its business activity outside a zone, which is not eligible. Reportedly, some taxpayers have placed simple storefronts in a zone, and then claimed the credit for business activity outside the

zone by manipulating the calculations. By altering the calculations in specific ways, the bill should end this practice and ensure that a credit claimed for business activity within a renaissance zone is legitimate.

The bill also amends the method by which the credit may be claimed for qualified business activity (related to the research and development of alternative energy systems within a zone). Even though this credit is not available until after 2002, the calculation of the credit also needed to be changed to prevent those without a legitimate basis for the credit from claiming it.

Legislative Analyst: George Towne
Julie Koval

FISCAL IMPACT

The bill will increase General Fund revenues by a likely minimal amount. The bill limits the credit that may be claimed for activities in a renaissance zone. The bill will affect credits under current law as well as the recently enacted credit for alternative energy activities. The bill attempts to limit the credits to reflect activity that actually occurs within or is reflected by the presence of the renaissance zone. The previous law apparently allowed some taxpayers to claim credits for amounts based upon more than the activity in the renaissance zones would suggest and more than was originally estimated given levels of activity within the zones.

For the existing renaissance zones, the bill will reduce some taxpayers' credits. The amount of revenue involved is not expected to be significant, but could total several million dollars. For those provisions affecting credits related to alternative energy activities, the bill will have no effect because no credits have been awarded and no tax revenue has been received from the zones, and the fiscal impact estimated for this credit assumed that it would accurately reflect the assumed level of business activity within the zones.

Fiscal Analyst: David Zin

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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.