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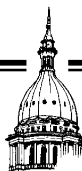
BILL  ANALYSIS

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Senate Bill 1037 (Substitute S-1) *(as passed by the Senate)*
Sponsor: Senator Jack Brandenburg
Committee: Finance

Date Completed: 5-23-12

CONTENT

The bill would amend the Michigan Business Tax (MBT) Act with respect to the business income tax base, the modified gross receipts tax base, the determination of sales in this State, the elimination of transactions between people in a unitary business group, and the calculation of several credits.

The bill states, "This amendatory act is curative and intended to clarify the original intent of 2007 PA 36" (the MBT Act).

Business Income Tax Base

The Act imposes a business income tax on taxpayers with business activity in the State at the rate of 4.95% of the business income tax base. The tax base is a taxpayer's business income subject to a number of adjustments. One of the adjustments allows the taxpayer to deduct, to the extent included in Federal taxable income, any earnings that are net earnings from self-employment, as defined in the Internal Revenue Code (IRC), of the taxpayer or a partner or limited liability company (LLC) member of the taxpayer, except to the extent that those net earnings represent a reasonable return on capital.

The bill, instead, would allow a taxpayer to deduct, to the extent included in business income, any earnings that were net earnings from self-employment as defined in the IRC of the taxpayer or a partner or LLC member of the taxpayer and that were reported to the taxpayer or a partner or LLC member on a Schedule K-1-Form 1065 as self-employment earnings for Federal income tax purposes.

The Act also allows a taxpayer to deduct any available business loss incurred after December 31, 2007. The bill provides that, for this purpose, a taxpayer that acquired the assets of another corporation in a transaction described in Section 381(a)(1) or (2) of the IRC could deduct any business loss attributable to that distributor or transferor corporation. (That section of the IRC pertains to carryovers in certain corporate transactions, and contains a general rule when the assets of one corporation are acquired by another in certain distributions or transfers.)

Modified Gross Receipts Tax

The Act imposes a modified gross receipts tax on taxpayers with nexus. The modified gross receipts tax base is a taxpayer's gross receipts less purchases from other firms before apportionment.

The definition of "purchases from other firms" includes materials and supplies, to the extent not included in inventory or depreciable property. The bill specifies that, for this purpose, materials and supplies would mean tangible personal property expensed by the taxpayer and not capitalized for Federal income tax purposes.

"Purchases from other firms" also includes assets acquired during the tax year of a type that are, or under the IRC will become, eligible for depreciation, amortization, or accelerated capital cost recovery for Federal income tax purposes. The bill would refer to assets acquired or self-constructed during the tax year of the specified type.

In addition, the bill would exclude from the definition of "gross receipts" amounts attributable to the taxpayer pursuant to a discharge of indebtedness as described in Section 61(a)(12) of the IRC, including forgiveness of a nonrecourse debt. (That section of the IRC includes in the gross definition of "gross receipts" income from discharge of indebtedness.)

Apportionment: Sales in this State

The Act requires the apportionment of a taxpayer's tax base based on the sales factor, which is the total sales of the taxpayer in this State divided by the total sales of the taxpayer everywhere during the tax year. Sales of the taxpayer in this State include sales of tangible personal property that is shipped or delivered to any purchaser within this State based on the ultimate destination at the point that the property comes to rest, regardless of the free on board point or other conditions of the sales.

The bill provides that, for purposes of determining the ultimate destination and when the property comes to rest, if the buyer did not identify the ultimate destination at the time of the transaction, property would be considered temporarily stored at that destination if it were stored for fewer than 30 days.

Unitary Business Group

The Act requires a unitary business group to file a combined return that includes each United States person, other than a foreign operating entity, that is included in the group. Each United States person included in a unitary business group or included in a combined return must be treated as a single person and all transactions between those people included in the group must be eliminated from the business income tax base, modified gross receipts tax base, and the apportionment formula under the Act.

The bill also would transactions between the people in the group to be eliminated for purposes of determining the exemptions, deductions, subtractions, credits, and filing threshold under the Act.

Credits

Section 403 of the MBT Act allows a compensation credit and a credit based on the cost of tangible assets, and requires these credits to be taken before any other credit under the Act. The bill would require the credits allowed under this section and Section 405 (which allows a research and development credit) to be taken before any unused carryforward allowed under Section 401 and before any other credit under the Act. (Section 401 allowed any unused carryforward for a credit under the former Single Business Tax Act (SBT) to be applied for the 2008 and 2009 tax years.)

The bill also would revise the calculation of the renaissance zone credit for a taxpayer located and conducting business activity in a renaissance zone before December 1, 2002, providing for the credit to be based on either the current calculation for those taxpayers, or

the calculation allowed for other business taxpayers in a renaissance zone, whichever was greater.

MCL 208.1111 et al. Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would reduce General Fund revenue by an unknown and likely significant amount. The provisions of the bill generally would: 1) exclude certain income and receipts from the tax base, 2) reduce the tax base by increasing the value of certain deductions, and 3) alter the calculation for computing or applying certain credits. While the impact of many of the changes is unknown, the Department of Treasury estimates that the changes in the definition of materials and supplies could reduce revenue by as much as $110 million per year, while the changes in the renaissance zone credit would lower revenue by approximately $11 million per year.

The intent language indicating the changes are curative suggests the bill is intended to be retroactive. To the extent the bill was retroactive, the loss of revenue would be increased by an unknown amount that would likely be substantially greater that if the bill were not retroactive. For example, because it would affect four years of returns, the change in the definition of materials and supplies could reduce revenue by as much as $440 million.

Because taxpayers could claim Single Business Tax (SBT) credit carry-forwards only in the 2008 and 2009 tax years, these changes in the bill would have an impact only if the bill were retroactive. The changes in the application of SBT credit carry-forwards could reduce revenue by as much as $20 million.

Most of the revenue loss from any retroactivity would likely occur in FY 2012-13, as taxpayers filed amended returns as a result of the bill.

The bill would not affect local unit revenue or expenditure.

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.