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BILL ANALYSIS

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House Bill 6485 (as reported without amendment)
Sponsor: Representative Triston Cole
House Committee: Commerce and Trade
Senate Committee: Finance

CONTENT

The bill would amend the Income Tax Act to list certain costs and allowances that would not be included as expenses of producing oil and gas for the purposes of calculating taxable income and the Corporate Income Tax (CIT) base.

Part 1 of the Act imposes a tax at the rate of 4.25% on the taxable income of individuals. "Taxable income" means adjusted gross income as defined in the Internal Revenue Code (IRC), subject to a number of additions and deductions. For tax years beginning after December 31, 2011, the term requires a person to eliminate from his or her adjusted gross income all of the following:

-- Income from producing oil and gas to the extent included in adjusted gross income.
-- Expenses of producing oil and gas to the extent deducted in arriving at adjusted gross income.

"Taxable income" in the case of a resident estate or trust means Federal taxable income as defined in the IRC, subject to a number of additions and deductions. For tax years beginning after December 31, 2011, the term requires a resident estate or trust to eliminate from its Federal taxable income all of the following:

-- Income from producing oil and gas to the extent included in Federal taxable income.
-- Expenses of producing oil and gas to the extent deducted in arriving at Federal taxable income.

Part 2 of the Act imposes the CIT on every taxpayer with business activity within Michigan or ownership interest or beneficial interest in a flow-through entity that has business activity in the State. The CIT is imposed on the CIT base, after allocation or apportionment to the State, at the rate of 6.0%. The CIT base is a taxpayer's business income subject to various adjustments, including, for tax years beginning after December 31, 2011, the elimination of all of the following:

-- Income from producing oil and gas to the extent included in Federal taxable income.
-- Expenses of producing oil and gas to the extent deducted in arriving at Federal taxable income.

Under the bill, as used in the provisions above, expenses of producing oil and gas would include costs allowable as a deduction from the sales price of the oil and gas in determining the gross cash value of the oil and gas at the wellhead for the severance tax, but would not include any of the following:

- -- Costs incurred to purchase, lease, or otherwise acquire an oil and gas property, whether proved or unproved.
- -- Costs incurred for exploration or development of an oil and gas property, whether producing or nonproducing.
- -- Costs incurred for processing, transportation, or marketing of the oil and gas that had been produced from an oil and gas property.
- -- Costs incurred for plugging and abandonment of an oil and gas property.
- -- Allowances for depletion that did not reduce the adjusted basis of the oil and gas property.

The bill also states the following: "This amendatory act is curative and intended to clarify the original intent of the legislature regarding the application of the deduction for certain income and expenses related to oil and gas as added by 2011 PA 38. Accordingly, this amendatory act is retroactive and effective for all tax years beginning after December 31, 2011."

MCL 206.30 et al. Legislative Analyst: Drew Krogulecki

FISCAL IMPACT

Based on information from the Department of Treasury, the bill would reduce corporate and individual income tax revenue by approximately $4.0 to $5.0 million per year. The retroactivity provisions of the bill also would reduce revenue by an additional $10.0 million in the first fiscal year in which the bill was in effect.

While all corporate income tax revenue is directed to the General Fund, gross individual income tax revenue is split between the General Fund and School Fund (currently the School Aid Fund receives 23.8% of gross individual income tax revenue) and all individual income tax refunds reduce General Fund revenue. The retroactive provisions would be expected to reduce General Fund revenue. For the ongoing provisions, the proportion of the bill's impact that would reduce School Aid Fund revenue is unknown.

Date Completed: 12-13-18 Fiscal Analyst: David Zin