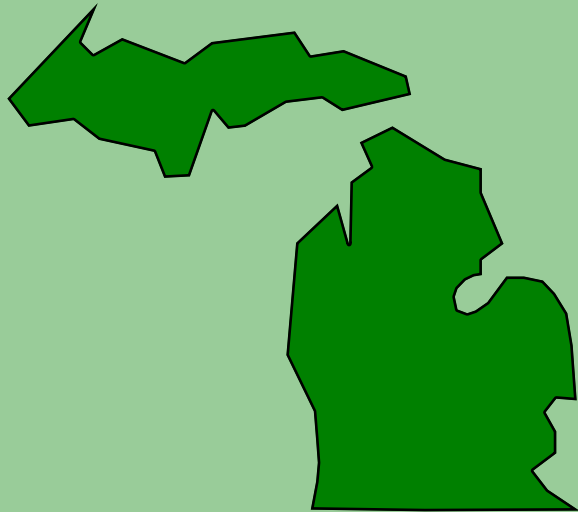


MICHIGAN BUSINESS TAX



Michigan Department
of Treasury

FOUR IN ONE

- **The Michigan Business Tax (MBT) is actually four taxes in one Public Act. It contains:**
- **Two general imposition provisions that apply to most business entities, and**
- **Two special imposition provisions that apply to insurance companies and to financial organizations.**

GENERAL IMPOSITION PROVISIONS

- **First, a 4.95% tax on a defined business income tax base,**

AND

- **Second, a 0.8% tax on a defined modified gross receipts tax base.**

SPECIAL INSURANCE COMPANY IMPOSITION PROVISIONS

- **A 1.25% tax on defined direct premiums or tax calculated under section 476a of the insurance code, whichever is greater.**

SPECIAL FINANCIAL INSTITUTION IMPOSITION PROVISION

- **A 0.235% franchise tax on net capital.**
- **Special single sales factor apportionment calculations are required.**



UNITARY GROUPS

UNITARY FOUNDATIONS

- **Under the unitary business principle, if a taxpayer is carrying on a single unitary business within and without the state, the state has the requisite connection to the out-of-state activities of the business to justify inclusion in the taxpayer's apportionable tax base of all of the property, income, or receipts attributable to the combined effect of the in-state and out-state activities.**

UNITARY IN THE MBT

- “Unitary business group” means:
 - A group of U.S. persons other than a foreign operating entity;
 - one of which owns/controls, directly or indirectly, more than 50% of the ownership interest of the other U.S. persons; and
 - that has business activities or operations that result in a *flow of value* between or among persons in the business group; or
 - that has business activities or operations that are *integrated with, are dependent upon, or contribute to* each other.

UNITARY IN THE MBT (CONT'D)

- **“Taxpayer” includes a unitary business group.**
- **A unitary business group shall file a combined return.**
 - **Must include each U.S. person other than foreign operating entities.**
 - **All transactions between persons included in the unitary business group must be eliminated from the business income tax base, the modified gross receipts tax base, and the apportionment formula.**
 - **Persons subject to the taxes under Chapters 2A and 2B of the MBT as insurance companies or financial institutions are excluded from the combined return.**

FOREIGN OPERATING ENTITIES

- A unitary group does not include a Foreign Operating Entity.
- “Foreign Operating Entity” is all of the following:
 - A U.S. person that would otherwise be a part of a unitary business group;
 - Has substantial operations outside the U.S. or any territory or possession;
 - At least 80% of its income is active foreign business income as defined by section 861(c)(1)(B) of the IRC.

UNITARY: FLOW OF VALUE

- “The prerequisite to a constitutionally acceptable finding of unitary business is a *flow of value . . .*” *Container*, 463 US 159 (1983).
- Common tests for identifying unitary business (and a flow of value) include:
 - Functional integration (same line of business or steps in a vertically integrated process);
 - Centralized management (actual control; centralized departments or functions);
 - Economies of scale (exists whenever a function is enhanced through the sharing of the group’s resources).

UNITARY: INTEGRATED, DEPENDENT, AND CONTRIBUTE

- **Alternate Test – (integrated, dependent, and contribute):**
 - **A taxpayer is engaged in a unitary business when its activities within the state contribute to or are dependent upon its activities without the state.**



BUSINESS INCOME NEXUS

SPECIAL BUSINESS INCOME NEXUS FOR SALES OF TPP

- *Tangible personal property (TPP)* sales are subject to the narrower PL 86-272 federal statutory jurisdictional standards, which provide that nexus does not exist if business activity in a state is limited to solicitation activities.
- Mere solicitation of TPP sales is insufficient to establish nexus.
- PL 86-272 is not applicable to receipts on “services” or “intangibles” which are subject to same nexus standard as for modified gross receipts.



BUSINESS INCOME TAX BASE

BUSINESS INCOME TAX BASE

- **Starting point: federal taxable income from business activity.**
- **Applies to all entity types.**
- **S corps & partnerships include in taxable income any income or expense attributed to business activity reported separately to partners or shareholders.**
- **No casual transaction exclusion.**

BUSINESS INCOME TAX BASE (CONT'D)

- **SBT modifications to tax base that have been deleted:**
 - **Compensation**
 - **Depreciation and capitalized expenses**
 - **Royalty and interest add backs**

BUSINESS INCOME TAX BASE (CONT'D)

- **SBT modifications to tax base that have been retained:**
 - **Dividends and interest received on obligations of other states.**
 - **Taxes on or measured by income**
 - **Federal net operating losses.**
 - **Income /losses from other entities subject to this tax.**
 - **Income from U.S. obligations.**

BUSINESS INCOME TAX BASE (CONT'D)

- **New modification to tax base:**
 - **Deduct net earnings from self employment included in federal taxable income unless they are a return of capital.**
 - **Add intangibles expenses included in federal taxable income made to related parties not part of the unitary group.**

BUSINESS INCOME TAX BASE (CONT'D)

- **Exceptions to intangibles expense add back:**
 - **Taxpayer must demonstrate transaction is not to avoid taxes.**
 - **Transaction was at arms-length.**
 - **AND satisfies one of the following:**

BUSINESS INCOME TAX BASE (CONT'D)

- The arms length transaction was:
 - A pass through from a 3rd party to the related person with comparable rates and terms, or
 - Would be taxed by another jurisdiction, or
 - Addition is unreasonable based on facts and circumstances.

UNITARY BUSINESS INCOME TAX BASE

- **Group files combined return – transfer pricing not allowed.**
- **Add tax bases of group members – apply combined apportionment %.**
- **Foreign operating entities, insurance companies, & financial institutions cannot participate.**

BUSINESS LOSS CARRYOVER

- **2008 1st year allowed – apportioned loss may be carried forward 10 years.**
- **Apportion in year incurred – carryover to next year after apportionment.**
- **Portion of unused SBT loss carryover used in gross receipts tax base.**



MODIFIED GROSS RECEIPTS TAX NEXUS

NEXUS

- Taxpayer has a *physical presence* for more than 1 day per tax year,

OR

- Taxpayer *actively solicits* sales and has MI gross receipts of \$350,000 or more.

NEXUS

- Physical presence means “*any activity*” by:
 - A taxpayer, or
 - its independent contractor, or
 - its representative.
- SBT RAB 1998-1 remains helpful for determining physical presence, but by its own terms is limited to SBT. A new MBT Nexus RAB will be developed.

NEXUS

- **Physical presence *exclusion* for:**
 - ***Professionals* providing services in a professional capacity, or**
 - ***Other service providers* if the activity is NOT associated with establishing a MI market.**

NEXUS

- **“Actively solicits” is to be defined by the department.**

- **Applied prospectively**

Note: Modified Gross Receipts Nexus standard differs from that of the business income tax portion of the MBT applicable to sales of tangible personal property.



MODIFIED GROSS RECEIPTS TAX BASE

MODIFIED GROSS RECEIPTS TAX BASE

- **Gross Receipts defined as:**
 - **The entire amount received by the taxpayer from any activity whether in intrastate, interstate, or foreign commerce carried on for gain to the taxpayer or others.**

MODIFIED GROSS RECEIPTS TAX BASE - EXCLUSIONS

- **Amounts received as an agent on behalf of the principal.**
- **Certain amounts realized from the sale of marketable instruments.**
- **Receipt of the loan principal by residential mortgage companies.**
- **Receipts by a professional employer organization of the cost of wages paid under the professional employer arrangement.**
- **Amounts received by auto dealers subsidizing interest expenses.**

MODIFIED GROSS RECEIPTS TAX BASE (CONT'D)

- The tax base is a taxpayer's gross receipts less "purchases from other firms" before apportionment.
- "Purchases from other firms" means:
 - Inventory acquired during the tax year.
 - Depreciable assets acquired during the tax year.
 - Materials and supplies, including repair parts and fuel.

MODIFIED GROSS RECEIPTS TAX BASE (CONT'D)

- Compensation of personnel supplied to customers of a staffing company.**
- Payments by contractors to subcontractors.**
- A unitary business group's modified gross receipts is the sum of each person's modified gross receipts in the group, less modified gross receipts from transactions between persons in the group.**

SBT LOSS CARRYFORWARD MODIFICATION

- **For tax year 2008, firms may deduct 65% of business loss carryforward left from the Single Business Tax Act, “actually incurred in the 2006 or 2007 tax year.”**
- **For a unitary group, the deduction may only be taken against the modified gross receipts of the person with the loss.**

CARS & BOATS

- **New motor vehicle and watercraft dealers may separately itemize the modified gross receipts tax on invoices to their customers and collect the tax in addition to the sales price.**
- **The amount remitted to Treasury for the tax cannot be less than the stated and collected amount.**

Note: Amounts separately itemized as modified gross receipts tax are subject to sales tax on taxable sales of motor vehicles and watercraft.



APPORTIONMENT

ALLOCATION AND APPORTIONMENT

- **Single factor apportionment based on sales.**
- **No throwback sales.**
- **Sales are sourced to another state if that state has jurisdiction to tax even if that state does not do so.**

SALES FACTOR

- **Formula: MI sales/sales everywhere**
- **“Finnegan” is applied to unitary groups when at least one person in the group has Nexus, all MI sales by persons in the unitary group are included in the numerator.**

SOURCING SALES OF TPP, ELECTRICITY AND GAS

- **Ultimate destination test is applied.**
- **Sourced to where property comes to rest regardless of shipping terms.**
- **Gas and electricity sourced based on where contract requires delivery.**

SOURCING OF REAL PROPERTY RECEIPTS

- **Real property is sourced where the property is located.**

SOURCING RECEIPTS OF TPP LEASES

- **Leased tangible personal property is sourced where the property is utilized.**
- **“Utilized” is determined by the number of MI rental days/rental days everywhere.**
- **Default is where lessee obtained possession of TPP.**

SOURCING RECEIPTS OF MOBILE PROPERTY

- **Leased mobile transportation property is sourced where property is used.**
- **Aircraft use is determined by MI landings/landings everywhere.**
- **Default is principal base of operations.**

SOURCING RECEIPTS OF ROYALTIES AND INTANGIBLES

- Royalties and intangibles are sourced where the property is used by the purchaser.
- Multistate use apportioned by MI use/use everywhere.
- Default-exclude from numerator and denominator.
- Customer location is irrelevant.

SOURCING RECEIPTS OF SERVICES

- **Service income is sourced where recipient receives the benefit.**
- **Multistate use apportioned by recipient's MI benefit/benefit everywhere.**
- **“Cost of performance” sourcing no longer applicable.**

OTHER SOURCING PROVISIONS

- **Securities brokerage service receipts are sourced to customer's address.**
- **Regulated investment companies receipts are based on shareholders domicile/ mailing address.**

OTHER SOURCING PROVISIONS (CONT'D)

- **Financing activities receipts (generally follow RAB 2002-14).**
- **Transportation receipts (generally sourced MI revenue miles/ revenue miles everywhere).**

OTHER SOURCING PROVISIONS (CONT'D)

- **Telecommunications receipts have several sourcing rules.**
- **Telecommunications terms follow the Streamlined Sales and Use Tax Agreement.**

SOURCING IN GENERAL

- **New default sourcing rule:**
 - **Where the benefit to customer is received.**
 - **If benefit received is undeterminable to customer's location.**

SOURCING

- **Retained alternative sourcing along lines of SBT section 69**
 - **Department's discretion.**
 - **Alternate method may only be used if department approves.**
 - **Statutory apportionment is presumed to represent activity.**
 - **Taxpayer has burden of proof.**
 - **Amended returns are not a petition for relief.**



INSURANCE COMPANY TAX BASE AND CREDITS

INSURANCE COMPANIES

- **In lieu of the modified gross receipts and business income taxes.**
- **1.25% of gross direct premiums written on property or risk located in MI.**

INSURANCE COMPANIES (CONT'D)

- **Some exemptions from the base – premiums not taken, canceled policies.**
- **\$190 million of disability insurance premiums, reduced if more than \$280 million in premiums (increased).**
- **No traditional apportionment because only premiums on MI risks and property are taxed.**

INSURANCE COMPANY CREDITS

- **Credits**
 - **Same as SBT**
 - **Association payments**
 - **50% examination fees**
 - **New Alternate Credit**
 - **Company that does not make association payments qualifying for credit may take a credit for the amount of MI compensation credit allowed under Section 403(2) up to 65% of tax liability after other credits allowed insurance companies.**

INSURANCE COMPANY CREDITS (CONT'D)

- **Same as SBT**
 - **Workers disability compensation payment credit.**
 - **Refundable within 60 days for insurance companies only.**
 - **Can also be used against estimated payments.**

FOREIGN INSURANCE COMPANY ALTERNATE TAX

- **Retaliatory Tax described in the insurance code.**
- **Identical to SBT provision.**



FINANCIAL INSTITUTION DEFINED

DEFINITIONS

- **About 20 additional new definitions for the MBT**
- **Financial Institution – limited to:**
 - **Banks**
 - **Thrift banks**
 - **Thrift institution**
 - **Savings and loan company**
 - **Any person owned directly or indirectly by a financial institution other than insurance company taxed under Chapter 2A**
 - **A unitary business group of these entities**



FINANCIAL INSTITUTION TAX BASE

FINANCIAL INSTITUTION TAX BASE

- **Net capital as computed by Generally Accepted Accounting Principles (GAAP);**
 - **The average of net capital for current tax year plus the past four years**
 - **Exception for new businesses**
 - **With certain listed exclusions:**
 - >**goodwill from purchase of accounting adjustments after 7/1/07**
 - >**U.S. and MI obligations**
 - **Guidance for the calculation in case of merger/acquisitions**



FINANCIAL INSTITUTION APPORTIONMENT

APPORTIONMENT FOR FINANCIAL INSTITUTIONS

- **Business activities confined within MI are allocated to MI.**
- **Within and without MI is apportioned by multiplying the tax base by the gross business factor.**
- **Gross business factor is total gross business in Michigan over total gross business everywhere.**
- **Gross business defined in Sections 261(g) and 269, and includes fees for financial services; gains from sales of loans, etc.; interest; and other receipts from financial operations.**
- **Gross business includes every member of a unitary group regardless of nexus with intercompany eliminations.**
- **Generally follows RAB 2002-14.**



CREDITS AND CREDIT CARRYOVERS

RETAINED CREDITS

- **Many SBT credits are retained under MBT (10 credits):**
 - **Start-up business credit**
 - **Michigan early stage venture capital voucher**
 - **Workers' disability compensation**
 - **Food bank and homeless shelter contribution**
 - **Next Energy**
 - **Renaissance Zone**
 - **Historic Preservation**
 - **Brownfield**
 - **Hematite**
 - **MEGA payroll**

SBT CREDITS NOT RETAINED IN MBT (11 CREDITS)

- **Public Utility Property Tax Credit**
- **Hybrid Technology R & D**
- **Pharmaceuticals**
- **Unincorporated Business Credit**
- **MEGA Business Activity Credit**
- **Enterprise Zone**
- **Apprenticeship**
- **Donated Auto**
- **Minority Venture Capital Credit**
- **Transferred Jobs Credit**
- **Created Jobs Credit**

CREDITS EXPANDED IN MBT

- **Some credits were retained but slightly expanded (2 credits):**
 - **Public contribution (expanded to include the Michigan housing and community development fund as a public institution)**
 - **Community foundation credit (expanded to include education foundations)**

CREDITS EXPANDED IN MBT (CONT'D)

- **More notable expansions (2 credits)**
 - ❖ **Alternate Credit**
 - **Qualifying thresholds have been increased:**
 - **Adjusted business income (ABI) limit was increased from \$475,000 to \$1.3 million.**
 - **Gross receipts limit increased to \$19-\$20 million from \$9-\$10 million.**
 - **Allocated income limit increased to \$160,000-\$180,000 from \$95,000-\$115,000.**
 - **Only the adjusted business income threshold is indexed to inflation.**
 - **Alternate tax rate is reduced to 1.8 percent from 2.0 percent.**

CREDITS EXPANDED IN MBT (CONT'D)

❖ Personal Property Tax Credit

- The 15 percent SBT industrial personal property tax credit is increased to 35 percent.
- Two new personal property tax credits are added:
 - 23 percent for State Utility personal property taxes (telephone property). Reduced to 13.5 percent in subsequent years.
 - 10 percent natural gas pipeline utility personal property tax credit.
 - Credits are refundable.

CREDIT CARRY FORWARDS FROM SBT

- **Unused SBT credits may be carried forward and applied against MBT liability for tax years 2008 and 2009 only -- unless specified separately.**
- **Historic Preservation and Brownfield carryforwards are available for the same period they would have been under the SBT.**

NEW MBT CREDITS

- **Notable new MBT Credits for activities in MI only:**
 - **Compensation Credit - Equal to 0.37 percent of MI compensation.**
 - **Investment Tax Credit - Equal to 2.9 percent of MI investment.**
 - **Research and Development - Equal to 1.9 percent of MI research and development expenses.**
 - **Credits are “less than non-refundable”**
 - **Sum of the compensation credit and investment tax credit cannot exceed 65 percent of MBT liability before credits.**
 - **Sum of all three cannot exceed 75 percent of MBT liability before credits.**

NEW MBT CREDITS (CONT'D)

- **Filing Threshold Credit**
 - Deals with the cliff introduced by the \$350,000 filing threshold alone.
 - The credit is equal to the amount by which the allocated or apportioned gross receipts are less than \$700,000 divided by \$350,000 times MBT liability.
 - The credit declines linearly (and tax liability increases linearly) as gross receipts increase -- instead of an all or nothing cliff.

NEW MBT CREDITS (CONT'D)

- **Other new credits (8 credits)**
 - **Research and Development MEGA Credit**
 - **NASCAR Speedway Credit**
 - **Stadium Credit**
 - **Arts and Culture Credit**
 - **Michigan Entrepreneurial Credit**
 - **New Motor Vehicle Dealer Credit**
 - **Two Michigan Headquartered Food Retailer Credits**



ADMINISTRATION

ADMINISTRATION

- **Tax administered pursuant the Revenue Act.**
- **Treasury must promulgate rules to implement the MBT.**



ESTIMATED RETURNS AND PAYMENTS

ESTIMATED RETURNS AND PAYMENTS



- Quarterly estimates due for taxpayer expecting tax liability to exceed \$800.
- Calendar year estimates due 4/15, 7/15, 10/15, and 1/15.
- Corresponding dates for fiscal filers and first year less than 12 months.
- Safe harbor (no interest) if 85% of tax liability and a reasonable approximation per quarter or, for tax year 2009 and after, if prior year's tax is \$20,000 or less, prior year's amount in 4 equal payments.
- 1% gross receipts safe harbor gone.



FIRST TAXABLE YEAR CALCULATION FOR FISCAL FILERS

FIRST TAXABLE YEAR CALCULATION FOR FISCAL FILERS

- **May elect one of the following:**
 - **Annual method, reporting the taxpayer's full year multiplied by a ratio of the number of months in the tax year included under the MBT over 12.**
 - **Actual method, reporting only those months included under the MBT.**



**ANNUAL/FINAL
RETURN,
EXTENSIONS,
FILING THRESHOLD**

ANNUAL/FINAL RETURN, EXTENSIONS

- **Due last day of 4th month after tax year end with payment of final liability.**
- **Extension by department for good cause with application and payment of tax due.**
- **Automatic extension if federal extension to last day of 8th month with copy of federal request for extension with tentative return and payment of estimated tax.**

FILING THRESHOLD

- **Taxpayers other than Insurance Companies or Financial Organizations not required to file or pay if apportioned gross receipts less than \$350,000.**
- **Filing threshold annualized for tax year less than 12 months.**

PORTION OF MBT EARMARKED TO SCHOOL AID FUND(SAF)

- In fiscal year (FY) 2007-2008, \$136 million collected will be distributed to the SAF. The balance goes into the general fund. In FY 2008-2009, \$479 million will go into the SAF. After FY 2009, the amount earmarked to the SAF is increased by the rate of inflation.
- **SBT Comparison:** All SBT revenue goes into the general fund.

SEVERABILITY CLAUSE

- **If a final order of a court of competent jurisdiction determines that any provision of this act that provides a deduction, credit, or exemption with respect to employment, person, services, investments, or other activity in the state is unconstitutional or applies to a similar activity outside of the state, that provision shall be severed and the remaining provisions would remain in effect.**

REVENUE LIMIT FOR MBT

- **If net cash payments exceed specified amounts for 2008, 2009 and 2010, half of excess goes to the Budget Stabilization Fund (BSF) and half is refunded on a pro rata basis.**
- **For 2008, net cash payments include SBT payments.**
- **Revenue from insurance companies is excluded from the calculation.**



QUESTIONS???