

14. *Entrepreneurial Credit.* For 2008, 2009, and 2010, a taxpayer may claim a credit equal to the taxpayer's MBT liability if the taxpayer had gross receipts of less than \$25 million, created at least 20 new jobs in the first year the credit is claimed, and made a capital investment of at least \$1.25 million in the state in the preceding tax year (the investment requirement is reduced to \$600,000 for subsequent years that the credit is claimed).
15. *Small R&D Business Startup Credit.* A business that conducts research and development and that has fewer than 25 employees and less than \$1 million in sales is entitled to credits equal to its MBT liability for up to five years if it has no business income but still has tax liability due to the modified gross receipts tax.
16. *Personal Property Tax Credit.* A taxpayer is entitled to the following credits:
- i) 35% of any taxes paid on eligible personal property during the year. Eligible personal property generally includes any property that is classified as industrial personal property.
 - ii) 23% of the amount paid in property taxes on eligible telephone personal property during 2008. Eligible telephone personal property is

personal property of a telephone company that is subject to personal property taxes. The credit amount is reduced to 13.5% for years after 2008.

- iii) 10% of the amount paid in property taxes on eligible natural gas pipeline property during the year.

Rebates

The law contains a revenue cap that limits the amount of tax that can be collected under the MBT. If the collections exceed this amount in 2008, 2009, or 2010, half of the excess will be returned to taxpayers in the form of a rebate. These limits do not apply to years after 2010.

Conclusion

We will keep you apprised of any further developments relating to the MBT in upcoming editions of Business Briefs. Please feel free to contact the business and tax attorneys at Bodman for further details regarding the MBT or to help plan the tax strategy for your business under the new law.

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Governor Signs New Michigan Business Tax Bill

On July 5, 2007, Governor Jennifer Granholm signed into law a package of bills creating the new Michigan Business Tax ("MBT"). The tax will take effect on January 1, 2008 for all business activity in the state occurring after December 31, 2007.

History

Michigan's former tax, the Single Business Tax ("SBT"), was the only value-added tax in the country. Because it was unique, complying with the SBT was complex and expensive. Being a value-added tax led to several unfortunate results: businesses could be stuck with a large tax liability even if they were not making a profit, and there was a disincentive to hire workers in Michigan because payroll deductions claimed for Federal tax purposes were added back in arriving at the SBT tax base.

General

The MBT is imposed on any business that has a physical presence in Michigan for more than one day during the year or if the business actively solicits sales in Michigan and has gross receipts of \$350,000 or more that are attributable to Michigan.

Taxpayers with gross receipts between \$350,000 and \$700,000 receive a credit that reduces their tax liability. The credit provides for a phase-in of the tax liability once a taxpayer reaches \$350,000 in gross receipts.

The tax is actually a combination of two different taxes, a business income tax and a gross receipts tax. The business income tax is imposed at a rate of 4.95% of a taxpayer's "business income tax base" apportioned to the State of Michigan. The modified gross receipts tax is imposed at a rate of 0.80% of a taxpayer's "modified gross receipts tax base" that is apportioned to Michigan. After the taxes are computed, businesses are eligible for several credits.

Although, the MBT is intended to be revenue neutral compared to the SBT, the MBT will change the distribution of tax liabilities. Generally, manufacturing firms would experience a tax liability reduction compared to the SBT, while nonmanufacturing firms

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would experience a tax increase. Similarly, while Michigan-only firms and multistate firms that are based outside of Michigan will generally experience liability increases, Michigan-based multistate firms will generally experience liability reductions.

Under the MBT, unitary business groups would be required to file a combined tax return. A unitary business group includes a group of businesses that is controlled by one of the businesses and that has activity or operations flowing between them. The stated goal of unitary filing is to eliminate potential tax abuses from intercompany transactions.

Property Tax Relief

In addition to the business tax changes brought about by the MBT, the Michigan personal property tax has been dramatically reduced. The personal property tax rate will be reduced by 12 mills for commercial property and 24 mills for industrial property. These reductions in the personal property tax will greatly benefit the manufacturing sector and other businesses that have substantial tangible personal property.

Alternative Taxes for Insurance and Banking

Businesses in the insurance and banking industries do not pay the business income tax and the modified gross receipts tax described above. Instead, the MBT sets forth special taxes that apply specifically to them.

Insurance companies pay a tax that is equal to 1.25% of the gross direct premiums written on property or risk located within Michigan. The company is permitted to exclude the first \$190 million of disability premiums written in Michigan. This exclusion is reduced if the company's gross direct premiums (both inside and outside Michigan) exceed \$280 million. Insurance companies may claim credits for various other taxes and fees paid in the state.

Financial institutions are subject to a franchise tax. The franchise tax is imposed on the tax base of the financial institution apportioned to Michigan, at a rate of 0.235%. The financial institution tax base is the net capital of the financial institution, calculated as a rolling five-year average. Net capital is the equity capital of

the institution less goodwill arising from purchase transactions that occur after December 31, 2007 and less the book value of United States and Michigan obligations.

Apportionment

As described above, the business income tax and the modified gross receipts tax are subject to apportionment if the taxpayer has business activities both inside and outside of Michigan. This apportionment of the MBT is determined entirely on a sales factor. The sales factor is calculated by dividing the Michigan sales of the taxpayer into the total global sales of the taxpayer for the given tax year.

Sales that are attributable to services are deemed to be Michigan sales to the extent that the recipient receives the benefit of the services in Michigan. Special apportionment rules for businesses operating in specific industries, such as brokerage and telecommunications, are provided for within the text of the bill.

Credits Against the MBT

The MBT carries over several credits previously applicable to the SBT. In addition, several new credits were created. Below is a summary of some of these credit provisions.

1. *Credit Carry-forward From the SBT.* The MBT permits a taxpayer to apply any unused SBT credit carry-forwards during the 2008 and 2009 tax years. After 2009, any remaining unused SBT credit carry-forwards will be lost.
2. *Compensation Credit.* A taxpayer is permitted to claim a credit equal to 0.370% of the compensation paid by the taxpayer in Michigan. "Compensation" means all wages, salaries, fees, bonuses, commissions, or other payments made in the tax year on behalf of or for the benefit of employees, officers, or directors of the taxpayer, and any earnings that are net earnings from self-employment of the taxpayer or a partner or limited liability company member of the taxpayer. This credit will not provide a full offset to the income that flows through to a partner, a shareholder of a S corporation or a member

of a LLC, which could therefore result in double taxation of some of the income generated by these types of entities.

3. *Small Business Credit.* A taxpayer that has gross receipts greater than \$350,000 but less than \$700,000 is eligible for a credit equal to the amount of tax imposed under the MBT. The amount of the credit is 100% of the tax liability if the taxpayer's gross receipts are \$350,000 and is 0% of the tax liability if the taxpayer's gross receipts are \$700,000. The tax credit is phased out ratably between these two amounts, in effect resulting in a graduated tax rate.
4. *Additional Small Business Credit.* A taxpayer that has gross receipts that do not exceed \$20 million and adjusted business income that does not exceed \$1.3 million is entitled to a credit that essentially permits the taxpayer to pay a flat tax of 1.8% of adjusted business income. This credit is only available if the compensation paid to certain key employees falls below certain disqualifying amounts. The credit is phased out for businesses that have gross receipts between \$19 million and \$20 million.
5. *Depreciable Asset Credit.* A taxpayer is permitted to claim a credit equal to 2.9% of the value of any depreciable property that is put into service and is located in Michigan for use in a business activity in Michigan, less the proceeds (net of any gain or loss) on the disposition of any depreciable property. Mobile assets are treated as used in Michigan in proportion to the sales apportionment factor used by the taxpayer to calculate its tax liability. If the credit is a negative number (because more property is retired from service than put into service), the negative credit will be treated as an additional tax liability.
6. *Research and Development Credit.* A taxpayer is permitted a credit equal to 1.90% of the taxpayer's research and development expenses within Michigan.
7. *Public Contributions Credit.* A taxpayer is permitted a credit equal to 50% of any contributions to public broadcasting stations; public libraries; institutions of higher learning; the Michigan colleges foundation; or the Michigan housing and community development fund. The amount of the credit cannot exceed the lesser of \$5,000 or 5% of the taxpayer's MBT tax liability.
8. *Museum and Zoo Credit.* A taxpayer is permitted a credit equal to 50% of the amount of any contributions in excess of \$50,000 to a museum or to a municipality or nonprofit organization affiliated with a municipality for the purposes of benefiting an art, historical, or zoological institute. The amount of the credit cannot exceed \$100,000.
9. *Community or Education Foundation Credit.* A taxpayer is permitted a credit equal to 50% of any contributions to the endowment fund of a community foundation or education foundation. The amount of the credit cannot exceed the lesser of \$5,000 or 5% of the taxpayer's MBT liability.
10. *Homeless Shelter and Food Bank Credit.* A taxpayer is permitted a credit equal to 50% of any contributions to a homeless shelter or food bank. The amount of the credit cannot exceed the lesser of \$5,000 or 5% of the taxpayer's MBT tax liability.
11. *Worker's Disability Compensation Credit.* A taxpayer is permitted a credit equal to the amount the taxpayer paid under the Worker's Disability Compensation Act for the tax year.
12. *Job Creation Credit.* The state will approve credits for up to 20 businesses per year that permit a credit equal to 30% of any eligible contributions from qualified taxpayers to the businesses, up to a maximum credit of \$300,000. The goal of the credit is to create jobs and to positively impact the local economy.
13. *MEGA Credit.* For companies that are expanding or relocating their businesses in Michigan, the MEGA credit that was used under the SBT continues under the MBT. Credits are permitted for up to 20 years.