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Michigan legislature approves MBT repeal, new corporate income tax, MTC apportionment prohibition

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On May 12, 2011, the Michigan Legislature gave approval to a three-bill tax package that would replace the Michigan Business Tax (MBT) with a 6 percent corporate income tax, effective January 1, 2012, and make other changes. The MBT would be repealed except for taxpayers electing to claim "certificated" credits under the MBT until those credits are exhausted. In addition, the legislature approved a measure that would bar taxpayers from apportioning income under the Multistate Tax Compact, effective January 1, 2011. [H.B. 4361, H.B. 4362, H.B. 4479, approved in Legislature 5/12/2011] Click here for a complete summary of the legislation.

Notably, "taxpayer" under the new corporate income tax would be limited to corporations. Thus, sole-proprietorships and flow-through entities that are subject to the MBT would not be subject to the corporate income tax. The new corporate income tax retains some of the features of the business income portion of the MBT: income tax would be apportioned under a single sales factor formula; sales of other than tangible personal property would be sourced to the state based on a market-based sourcing standard; a Finnigan sourcing rule would apply to unitary groups, and unitary groups would have to file combined returns. Like the MBT, nexus would be established if the taxpayer has physical presence in the state for a period of more than one day during the tax year or if the taxpayer actively solicits sales in the state and has sales of $350,000 or more that are sourced to the state. Credits allowed under the MBT would not be retained, with the exception of the "alternate tax credit" for taxpayers with gross receipts that do not exceed $20 million and adjusted gross income does not exceed $1.3 million. House Bill 4362 would allow taxpayers to remain subject to the MBT if they wish to claim certain "certificated" credits.

The tax regimes currently in existence under the MBT for insurance companies and financial institutions would be retained. Thus, insurance companies would continue to be subject to the greater of a tax imposed at the rate of 1.25 percent of gross direct premiums written on property or risk located or residing in this state or the retaliatory tax. Financial institutions would be subject to tax based on net capital at a rate of 0.29 percent.

As part of the tax package, the exemption for pension income is limited to $20,000 ($40,000 for a joint return) for taxpayers born in 1946 through 1952, and eliminated for taxpayers born after 1952. Other deductions pertaining to retirement income would be eliminated, and the legislation would make other personal income tax changes.

PwC Observes

"The tax package, as approved by the Legislature is consistent with prior versions of the bill," explains James Manley, SALT Managing Director with PwC in Detroit.

"Significantly, the FAS 109 deduction that existed under the MBT is not included in the legislation, despite heavy lobbying for the modification from business and industry groups. This could have a significant, negative financial statement impact for some taxpayers. Furthermore, the provision barring allocation and apportionment under the Multistate Tax Compact is 'effective January 1, 2011' and is not retroactive. Taxpayers should consider whether this provides an opportunity to make the election for prior years to apportion under the MTC equally-weighted three factor formula," suggest Manley.

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