



Grand Rapids Area Chamber of Commerce
Creating Opportunities for Business Success

**SINGLE BUSINESS TAX AND PERSONAL
PROPERTY TAX REPLACEMENT ALTERNATIVE**



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SINGLE BUSINESS TAX AND PERSONAL PROPERTY TAX
REPLACEMENT ALTERNATIVE

**Adopted by the Grand Rapids Area Chamber of Commerce Board of Directors,
September 19, 2006**

RECOMMENDED BY

Grand Rapids Area Chamber of Commerce Tax and Regulatory Affairs Committee

EXECUTIVE SUMMARY

The Grand Rapids Area Chamber of Commerce (GRACC) Tax and Regulatory Affairs Committee met numerous times over the past eight months to study alternative business tax plans for the replacement of the Michigan Single Business Tax (SBT) and Personal Property Tax (PPT). As a result, the Committee submits the following recommendation.

The guiding principles used in the development of the GRACC position include:

Broad tax base

Low-rate

Hard to circumvent

Treat all business sectors equally

Should not distort economic behavior

Nexus standards should benefit Michigan based businesses

Simple to administer

Included personal property tax repeal or relief to the extent possible

Existing credits/incentives must be honored and applied to the “New Tax”

GOAL

The goal of the Grand Rapids Area Chamber of Commerce is to create a net business tax reduction, with replacement revenues not to exceed 90% of the current revenue.

RECOMMENDATION

The Grand Rapids Area Chamber of Commerce supported the accelerated repeal of the SBT and the full elimination of the PPT. These business taxes need to be eliminated and replaced with an alternative plan, to make Michigan more competitive in retaining and attracting businesses. The Legislature has also recognized the negative effects of the SBT by voting to accelerate the repeal of the SBT by January 1, 2008. Many citizens have demonstrated their support for the accelerated SBT repeal through the signing of petitions for a legislative override. Specifically, 291,741 signatures were certified through the Michigan Secretary of State's office.

Michigan's SBT was unique as the only value added tax levied in the United States. The Grand Rapids Area Chamber of Commerce was one of the first business organizations to oppose the SBT upon its inception in 1975. We maintain that the SBT was an onerous and complicated tax, acting as a disincentive for further economic growth. Additionally, there is a growing trend among states to fully eliminate their personal property tax and Michigan has to act now to compete in the future. On June 21, 2005, recognizing that it penalizes business investment in equipment and machinery, the Grand Rapids Area Chamber of Commerce Board of Directors expressed its support for the complete elimination of the PPT.

In light of our opposition of the SBT and PPT, the Chamber recognizes the importance of a replacement revenue source for a portion of the SBT and PPT revenue. Therefore, the Tax and Regulatory Affairs Committee recommends replacing these two burdensome taxes with new, simplified tax structure through a Business Activities Tax.

REPLACEMENT RECOMMENDATION – MICHIGAN BUSINESS ACTIVITIES TAX (MBAT) PROPOSAL

Title: Michigan Business Activity Tax (BAT)

Nature of Tax: Tax on Michigan Business Activity (measured by Michigan sales or service revenue, less the cost of tangible personal property purchased for resale, manufacturing, leasing or the cost of funds for financial institutions.)

Approximate Current Revenue

- Single Business Tax - \$2.131 Billion
- Personal Property Tax - \$1.788 Billion

Total- \$3.919 Billion

Note: Revenues are based on the 2006 House and Senate Fiscal Agency's Consensus Revenue Forecast for FY 2007

Replacement Plan

The GRACC proposes that the “new” tax structure for Michigan businesses be a broad based low rate tax on business activity, although allowing for a flat fee for filers with under \$350,000 in gross revenue. Total replacement revenue can be estimated based on the approximate state private industry Gross Domestic Product. A Michigan BAT, for the purposes of replacing the SBT and PPT, shall incorporate the following measures:

- Subject to Revenue Act Administrative Audit and Appeal Procedures
- Business liability will be determined by a tax payer’s Michigan business activity, less their returns/allowances and apportioned purchases of tangible personal property for resale, manufacturing, leasing or the cost of funds for financial institutions.
- The MBAT will not be an income tax. Therefore, the Commerce Clause Nexus Standard should be applicable.
- Michigan Activity,
 - In general, tangible personal property sales would be sourced based on destination (Dock sales and shipping terms would have to be defined).
 - Sales to be defined as under current section 208.7 of the Single Business Tax Act.
 - For sales other than tangible personal property –based on the market (e.g. place where benefit is delivered).
 - There will have to be a formula developed to determine market based income.
 - Business activity will be determined on a single entity basis, however a taxpayer may elect to file consolidated. (Similar to Ohio)
 - Consolidated is determined by common ownership.
 - Consolidated group must include all entities under common control, even if a member does not have nexus with Michigan. Can elect to include foreign entities (non-US) as well.
 - Consolidated Group will be allowed to exclude activity between its members.
 - The election shall be a five year election.
- A single rate, not to exceed 0.75% would be applied.
- There will be a deduction for the greater of \$350,000 or the purchases of tangible personal property, for purposes of resale, manufacturing, leasing

or cost of funds for financial institutions. For multi-state company's, the deduction is subject to single factor apportionment based on sales.

- For tax payers with business activity of less than \$350,000:
 - Flat fee of \$150, for businesses with at least one employee.
 - Note: In years when productivity and receipts in Michigan exceed Michigan Department of Treasury's estimates, a credit may be received the following year (e.g. Oregon).

Economic Development Incentives / Credits

The GRACC recognizes the important role incentives play in furthering economic development in local communities throughout Michigan. The GRACC supports the current incentive and credits associated with specific economic development projects throughout the State. Therefore, any replacement of the SBT and PPT should incorporate provisions that allow for the utilization of previously granted credits / incentives and loss carryovers subject to the specific program requirements, limitations and sunsets. While the GRACC understands the continuing need to attract new businesses / industries and the need for economic development incentives in Michigan, it believes the new tax code should remain clear of any (targeted) credits (other than previously mentioned) that would be applied against the BAT or its tax base. It is the GRACC's position that all new incentives / credits issued by the state or local units of government shall be structured in the form of Cash Grants administered through the Michigan Economic Development Corporation or any future state economic development agency.

Any grant program must likewise incorporate accountability and substantiation of measurable goals or commitments on the part of the recipient. By providing the grants in installments, the state will have the ability to monitor the recipient's progress toward its stated commitments. The awarding of grants will come from a legislatively established fund, the balance of which is to be determined annually.

While the awarding of grants will be discretionary, those applying will need to meet an established set of criteria for application to the program. The GRACC recognizes incentives are necessary for more than job creation, such as Brownfield redevelopment. It is anticipated the Cash Grant Program will incorporate many existing incentive programs currently in place.

Performance targets will vary based on the specific program as discussed above. This example is merely for presentation purposes. The GRACC recognizes the growth of the economy in Michigan is based on good paying jobs that do not create a further drain on Human Service resources, therefore wage levels and benefits would need to be evaluated in more detail prior to the establishment of criteria.

For example, based on a \$100,000 incentive / cash grant:

- Performance measures
 - Create 25 jobs;
 - Average payroll salary of new jobs must be at least 25% above the minimum wage (\$12/hour) and appropriate level of employee benefits:
 - Grants to occur in quarters (25% at a time TBD)
 - Could utilize the existing MEGA Grant structure, within the Michigan Economic Development Corporation, for the administration of the cash grant program.

Distribution of Revenue (State and Local Units of Government)

With the repeal of the personal property tax, which is directly attributed to the funding of local units of government, the GRACC plan recommends they remain “whole” and receive a new revenue distribution with the following guidelines:

- Within the BAT, add a schedule (such as "L" for local) supplemental local tax rate to replace the PPT revenue.
- Start with the tax base from the return, and multiply by a *to be defined* local tax rate, to get the total local tax.
- Apportion the local tax among the local municipalities where the taxpayer has business activity using a two-factor apportionment formula, property and payroll, similar to the one currently used for the renaissance zone exemption. Pressure will be taken off the locals as this will only affect apportionment, not the amount of tax.
- After determining a tax payer’s total liability, the tax payer will send a copy of the return, and a check for the apportioned tax, to each local municipality.
- The Michigan Department of Treasury will be responsible for the auditing and all other compliance. Adjustments made to the state return automatically apply to the local portion of the tax.
- The Michigan Department of Treasury will arbitrate disputes among municipalities over the apportionment. Treasury and the municipalities will have to agree on specific depreciation tables, etc.

State Spending Reductions (Restructuring of Government)

The GRACC’s position recommends replacement revenues not to exceed 90% of the current state revenues. The GRACC MBAT Plan is designed to attract new and grow existing businesses in Michigan, resulting in increased future revenue. However, we support increased efficiencies and streamlining within state government. We recommend and would support any of the following measures to reduce state spending:

- Reduce barriers and create incentives for the consolidation of Governments,
- Reduce barriers and create incentives for the consolidation of School Districts,
- Competitive bidding for public school employees health insurance premiums,
- Move public school employees out of a Defined Benefit to a 401-K style retirement plan,
- Repeal the “prevailing wage” law for school construction projects,
- Sharing of local governmental unit services - across boundary lines,
- Medicaid Reform:
 - Support of a federally authorized waiver – allowing the state of Michigan to launch new creative pilot programs,
 - Increased incentives for Medicaid recipients to take care of themselves
 - Increased co-payments,
 - Re-prioritization of services – prioritize the procedures offered versus individuals,
- Welfare Reform:
 - Institute a threshold for the amount of time a recipient can receive benefits,
- Adopt legislation to preempt local units of government from adopting “living wage” ordinances,
- Explore new ways to penalize “non-violent” criminals to avoid over crowding jail / prison populations.

GRACC’s MBAT Revenue Recommendations

The attached MBAT revenue calculation is based on the Michigan Department of Treasury’s 2000 Gross Sales Information for SBT Filers. The model is broken down by the Standard Industry Codes (SIC). We assume that intangible income is not included in the numbers. The methodology behind the model below incorporates the following:

- The model assumes a \$350,000 tax threshold, however, a \$150 fee would be charged to all tax payers under \$350,000 in total sales, with at least one employee. State estimate in 2000-2001 information from 50,000 firms unavailable – assumed to be below threshold – possible \$14 million in revenue.
- If more revenue is brought in than budgeted – after a *to be determined* level is reached – a credit could be given on the following year return or be allocated to a

established Budget Stabilization Fund– not a rate reduction and make the calculation statutory to avoid conflicts (e.g. Oregon).

- Gross sales will exclude narrowly defined casual sales and casual investments of individual or other entities not engaged in business. Not for profits shall also be excluded.
- The methodology behind our model is: calculate the Michigan receipts by SIC code, multiply the Michigan receipts by a broad industry specific tangible personal property percentage of sales, multiplied by a *recommended* general tax rate.
- The GRACC plan calculates different tangible personal property deduction percentages based on industry.

SUMMARY SHEET

MICHIGAN BUSINESS ACTIVITIES TAX (MBAT)

Guiding Principals:

- Broad tax base
- Low rate
- Hard to circumvent
- Should not distort economic behavior
- Simple to administer
- Include personal property tax repeal or relief to the extent possible

Current Michigan Business Taxes:

- Single Business Tax;
 - Value added tax;
 - Michigan is the only state in the nation with such a tax;
 - Taxes healthcare, payroll and investment;
- Personal Property Tax;
 - Michigan is one of 30 states with the tax and the growing trend is to eliminate it (Ohio recently repealed);
 - Taxes investment in equipment and machinery;

Replacement Plan:

- Modified Gross Receipts Tax—Michigan Business Activities Tax (MBAT)

MBAT Details:

- Provides a replacement recommendation for the Single Business Tax and Personal Property Tax;

- Creates a net business tax reduction, with replacement revenues not to exceed 90% of the current revenue;
- The plan is broad based with a single low rate not to exceed 0.75% on **business activity**;
- **Business Activity** is defined as Michigan sales/service revenue, minus the cost of tangible personal property for the purposes of:
 - Resale, Manufacturing, leasing, or the cost of funds for financial institutions;
- Recommends a flat fee of \$150 for businesses with under \$350,000 in gross revenue;
- Provides a deduction for the greater of \$350,000 or the purchases of tangible personal property as identified above;
 - For multi-state company's, the deduction is subject to single factor apportionment based on sales;
- Maintains the integrity of previously granted economic development incentives/credits associated with existing projects throughout the State;
- Future development incentives should be given on a cash grant basis;
- Hold local units of government harmless;
- Recommends reductions in state spending (e.g. Medicaid Reform, Reduce barriers and create incentives for the consolidation of Governments/Schools).

Key Industries Impacted (Positive / Negative):

- Manufacturing, Retail, Professional Services, Insurance, Financial Institutions, and Local Units of Government;

Tax and Regulatory Affairs Committee Participants:

- **Alticor**, Beene Garter, **City of Grand Rapids**, **Consumers Energy**, David Barrons CPA, Dykema Gossett PLLC, Echelbarger Himebaugh Tamm & Co. P.C., **Grand Valley Metro Council**, **Meijer**, Pranglely Marks LLP, **The Rapid**, **The Right Place Inc.**, **Spartan Stores**, **Star Truck Rentals**, **Steelcase**.

Revenue Replacement Recommendation for the Elimination of the SBT and PPT

<u>Industrial Classification</u>	<u>Number of Firms</u>	<u>Percent of Firms</u>	<u>Michigan Receipts</u>	<u>Percent of Total MI Receipts</u>	<u>Estimated Tangible Personal Property as a percentage of sales</u>	<u>Tangible Personal Property for Purchases</u>	<u>Tax Rate Applied</u>	<u>Estimated BAT</u>
Agriculture, Forestry & Fishing	1,600	1.48%	\$2,298,369,457	0.38%	0.00%	\$0	0.750%	\$17,237,771
Mining	324	0.30%	\$3,245,006,054	0.53%	25.00%	\$811,251,514	0.750%	\$18,253,159
Construction	11,976	11.06%	\$35,413,044,314	5.82%	25.00%	\$8,853,261,079	0.750%	\$199,198,374
Manufacturing:	12,809	11.83%	\$143,825,097,980	23.65%	35.00%	\$50,338,784,293	0.750%	\$701,147,353
Other Durable Manufacturers	4,813	4.45%	\$33,406,131,115	5.49%	0.00%	\$0	0.750%	\$250,545,983
Non-Durable Manufacturers	2,959	2.73%	\$40,632,894,991	6.68%	0.00%	\$0	0.750%	\$304,746,712
Primary Metals	498	0.46%	\$9,406,906,284	1.55%	0.00%	\$0	0.750%	\$70,551,797
Fabricated Metals	1,995	1.84%	\$11,990,865,619	1.97%	0.00%	\$0	0.750%	\$89,931,492
Machinery - Except Electrical	1,919	1.77%	\$12,974,525,952	2.13%	0.00%	\$0	0.750%	\$97,308,945
Transportation Equipment	625	0.58%	\$35,413,774,019	5.82%	0.00%	\$0	0.750%	\$265,603,305
Transportation	2,957	2.73%	\$10,132,648,428	1.67%	0.00%	\$0	0.750%	\$75,994,863
Communications and Utilities	1,143	1.06%	\$24,371,503,811	4.01%	0.00%	\$0	0.750%	\$182,786,279
Wholesale Trade	4,643	4.29%	\$49,681,132,369	8.17%	32.00%	\$15,897,962,358	0.750%	\$253,373,775
Retail Trade	27,583	25.48%	\$159,676,298,422	26.25%	40.00%	\$63,870,519,369	0.750%	\$718,543,343
Finance, Insurance and Real Estate	8,456	7.81%	\$56,925,929,133	9.36%	0.00%	\$0	0.750%	\$426,944,468
Services	31,521	29.12%	\$103,538,968,217	17.02%	0.00%	\$0	0.750%	\$776,542,262
<u>Not Elsewhere Classified/Miscellaneous</u>	<u>5,242</u>	<u>4.84%</u>	<u>\$19,108,462,934</u>	<u>3.14%</u>	<u>0.00%</u>	<u>\$0</u>	<u>0.750%</u>	<u>\$143,313,472</u>
Totals	108,254		\$608,216,461,119			\$139,771,778,612		\$3,513,335,119

* The above model is to be treated as an estimate.
** Michigan Receipts are based on 2000-2001 Michigan Department of Treasury numbers.
** The tax rate applied is subject to adjustment for specific industries as actual figures become available.