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Business Strategists & Certified Public Accountants

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Use Tax on Services is Finally Repealed – Major Revisions to the Michigan Business Tax Act

GRAND RAPIDS, MI – Monday, December 3, 2007 – Over the weekend, the House of Representatives, the Michigan Senate, and Governor Jennifer Granholm's administration finally got together to repeal the much hated Use Tax on Services. Public Act 145 of 2007 is law. It repeals the Use Tax on Services and makes significant changes to the Michigan Business Tax.

At approximately 10:30 PM Friday night, an hour and a half before the tax was scheduled to go into effect, the Senate, House of Representatives and Governor reached an agreement on a replacement for the expanded Michigan Use Tax. It was the month-long debate on the replacement, how much, and how long, that held up the repeal.

In the early morning hours of Saturday, after the tax went into effect, the Senate recalled House Bill 5408 from conference committee, concurred in a substitute (S-8) and gave the measure immediate effect around 5:00 AM Saturday – five hours after the service tax went into effect. The Senate adjourned until next week Tuesday, December 4th.

The House of Representatives convened at 3:30 PM Saturday afternoon in special session to immediately consider the legislation. After an hour of caucus meetings, the House, on a 66 to 42 vote, passed the legislation.

Enrolled House Bill 5408 was presented to Governor Granholm at 4:55 PM, approved at 5:10 PM, and was filed with the Secretary of State at 5:20 PM on Saturday. The enrolled bill was assigned Public Act 145 of 2007 with immediate effect.

The legislation does three things:

Enacts Section 1. Repeals three sections of the Management of Budget Act.

Enacts Section 2. Repeals Section 3d of the Use Tax Act which expanded the imposition of the use tax on services, made it retroactive and effective immediately.

Enacts Section 3. Amended the Michigan Business Tax Act by adding two new sections and amending 14 other sections.

Michigan Business Tax Changes

The lost revenue from the repeal of the Use Tax on Services (PA 36 of 2007) will be replaced entirely by adjustments to the Michigan Business Tax Act (MBTA). The revenue is enhanced by the imposition of a surcharge and further limitations on the compensation credit, investment tax credit, and the research and development credit. Several other sections were amended.

New Section 281 - Surcharge

The new section 281 imposes a surcharge in the amount of 21.99%. The surcharge is imposed as a percentage of the taxpayer's tax liability after allocation and apportionment but before credits. The surcharge for a financial institution is 27.7% for tax years ending in 2008 and 23.4% for tax years ending after 2008.

The surcharge is not imposed on insurance companies subject to the tax imposed under Chapter

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2A of the MBTA or financial institutions authorized to exercise only trust powers subject to the tax imposed under Chapter 2B of the MBTA.

The surcharge will sunset after January 1, 2017 if the Michigan personal income growth exceeds certain statutory percentage figures in any one of the three years preceding 2017. The surcharge is capped at \$6,000,000 for any taxpayer for any single tax year.

New Section 451 – Beverage Container Deposit Law Credit

A distributor or manufacturer who originates a deposit on a beverage container may claim a credit against the Michigan Business Tax equal to 30.5% of expenses incurred during the tax year to comply with the bottle deposit law. The credit percentage drops to 25% in a year where the Section 281 surcharge is not imposed.

The credit is not refundable and any unused credit cannot be carried forward.

Amended Section 105(2) – Business Income

Business income for an individual, estate, trust or partnership organized exclusively for estate or gift planning purposes is limited to that part of federal taxable income derived from transactions, activities, and sources in the regular course of the taxpayer's trade or business.

Such income includes the following:

- A. All income from tangible and intangible property including the acquisition, rental, management or disposition of the property if an integral part of the taxpayers trade or business operations
- B. Gains or losses from stocks and securities of any foreign or domestic corporation and dividends and interest income if incurred in the taxpayer's trade or business
- C. Income derived from isolated sales, leases, assignment, licenses, divisions, or other infrequently occurring dispositions, transfers, or transactions involving property if the property was used in the taxpayer's trade or business, and
- D. Income derived from the sale of a business

Income excluded from business income for an individual, estate, trust or partnership organized exclusively for estate or gift planning purposes includes, but is not limited to the following:

- A. Personal investment activity, including interest, dividends, and gains from a personal investment portfolio or retirement account, and
- B. Disposition of tangible, intangible, or real property held for personal use and enjoyment, such as a personal residence or personal assets.

Amended Section 111(1) – Gross Receipts

The definition of gross receipts was amended by adding a new subsection "v" to subparagraph 1 for an individual, estate, trust or partnership organized exclusively for estate or gift planning purposes. Amounts received other than those from transactions, activities, and sources in the regular course of the taxpayer's trade or business are excluded from gross receipts.

The following amounts received are excluded from gross receipts:

- A. Receipts from tangible and intangible property including the acquisition, rental, management or disposition of the property if an integral part of the taxpayers trade or business operations
- B. Receipts received from stocks and securities of any foreign or domestic corporation and dividends and interest income in the course of the taxpayer's trade or business
- C. Receipts derived from isolated sales, leases, assignment, licenses, divisions, or other infrequently occurring dispositions, transfers, or transactions involving property if the

property is or was used in the course of the taxpayer's trade or business, and

D. Receipts derived from the sale of a business

Receipts excluded from gross receipts for an individual, estate, trust or partnership organized exclusively for estate or gift planning purposes includes, but is not limited to the following:

- A. Personal investment activity, including interest, dividends, and gains from a personal investment portfolio or retirement account, and
- B. Disposition of tangible, intangible, or real property held for personal use and enjoyment, such as a personal residence or personal assets.

Amended Section 113(6) – Purchases From Other Firms

The definition of purchases from other firms was amended by adding a new subsection (f) for film rental or royalty payments paid by a theater owner to a film distributor, a film producer, or a film distributor and producer.

For the 2009 tax year, the credit is equal to 50% of the film rental or royalty payments paid. For the 2010 tax year and each year thereafter, the credit is equal to all film rental and royalty payments paid.

Amended Section 201(2)(i) – FAS 109 Adjustment

The FAS 109 adjustment was amended to clarify that the adjustment provided for in Section 201(2)(i) is intended to flow through and reduce the surcharge imposed and levied under Section 281.

Amended Section 403(1) – Compensation Credit Limitation

The compensation credit was originally limited to 65% of the tax liability before credits. The amendment to Section 403(1) reduces the limitation to 50% for the 2008 tax year and 52% for the 2009 tax year and each year thereafter. The limitation is imposed on the tax liability before the imposition and levy of the surcharge under Section 281 and before all other credits.

Amended Section 403(2) – Compensation Credit Percentage

The compensation credit was originally 0.370% of the taxpayer's compensation in Michigan. The amendment to Section 403(2) reduces the percentage amount to 0.296% for the 2008 tax year only. For the 2009 tax year and each tax year thereafter, the credit percentage remains at 0.370%.

Amended Section 403(3) – Investment Tax Credit Percentage

The investment tax credit was originally 2.9% of the taxpayer's net acquisitions in Michigan. The amendment to Section 403(3) reduces the percentage amount to 2.32% for the 2008 tax year only. For the 2009 tax year and each tax year thereafter, the credit percentage remains at 2.9%.

Amended Section 405 – Research and Development Credit Percentage

The research and development credit was originally 1.9% of the taxpayer's research and development expenses in Michigan. The amendment to Section 405 reduces the percentage amount to 1.52% for the 2008 tax year only. For the 2009 tax year and each tax year thereafter, the credit percentage remains at 1.9%.

Amended Section 405 – Research and Development Credit Limitation

In the original MBTA, the combination of compensation credit, investment tax credit and the research and development credit could not exceed 75% of the total tax liability. The amendment to Section 405 reduces the limitation amount to 65% of the tax liability before the imposition and levy of the surcharge under Section 281.

Amended Section 409 – Michigan International Speedway Credit

The credit provided in Section 409 was expanded by adding a new Subsection 2. In addition to the credit previously allowed for infield renovation, grandstand and infrastructure upgrades and any other construction and upgrades, Section 409 was amended to provide a credit equal to 50%, for the 2008 tax year, of the amount of necessary expenditures incurred including any professional fees, additional police officers, and any traffic management devices, to ensure traffic and pedestrian safety while hosting the requisite motorsports events in each calendar year.

For the 2009 tax year and each tax year after 2009, the credit is equal to all of the necessary expenditures incurred including any professional fees, additional police officers, and any traffic management devices, to ensure traffic and pedestrian safety while hosting the requisite motorsports events in each calendar year.

The credit is refundable.

Amended Section 413 – Personal Property Tax Credit

The definition of property taxes qualifying for the credit was expanded to include taxes levied under the utility property tax statutes.

Amended Section 445 – New Motor Vehicle Dealer Credit

The new motor vehicle dealer credit was equal to 2% of the amount paid by the taxpayer to acquire new motor vehicle inventory in the tax year limited to \$10,000. The amendment to Section 445 reduced the credit percentage to 0.25% and eliminated the \$10,000 limitation.

Amended Section 447 – Meijer Grocery Store Credit

The section 447 additional compensation credit was increased from 0.535% to 1.0%. The limitation on the credit was increased from \$4.5 Million to \$8.5 Million.

Revenue Limits

The original MBTA limited revenue from the Michigan Business Tax starting in the 2008 state fiscal year through the 2010 state fiscal year. The MBTA specified that half of the excess revenue above the revenue limit would be deposited in the Budget Stabilization Fund and the other half be returned to taxpayers. Significant amendments were made to the revenue limitation provisions.

Amended Section 515 – School Aid Fund Revenue Designation

For the fiscal year 2007-2008 the amount of revenue designated for the school aid fund was increased from \$136,000,000 to \$341,000,000. For the fiscal year 2008-2009 the amount of revenue designated for the school aid fund was increased from \$479,000,000 to \$729,000,000.

The excess is deposited into the general fund. For each fiscal year after the 2008-2009 fiscal year, the amount from the previous fiscal year will be adjusted by an amount equal to the growth in the consumer price index.

Amended Section 601 – Revenue Limits

For the 2008 fiscal year, the revenue limit \$2,398,000,000 was deleted and replaced by a new computation of fiscal year 2008 base. The fiscal year 2008 base is calculated by multiplying \$2,619,100,000 by 1.0075 and then multiplying the product by the United States Consumer Price Index for the fiscal year 2008 and then dividing the product by the United States Consumer Price Index for the fiscal year 2007.

Revenue includes the total net cash payment from both the Single Business Tax and the Michigan Business Tax, but excluding revenue from the tax on insurance companies.

For the 2008 fiscal year, if the net cash payments exceed the fiscal year 2008 base, 60% of the

excess, an increase from 50%, will be refunded to taxpayers in the succeeding fiscal year and the remaining 40%, a decrease from 50%, will be deposited into the budget stabilization fund. For the 2009 fiscal year, if the net cash payments exceed the fiscal year 2009 base, 60% of the excess, an increase from 50%, will be refunded to taxpayers in the succeeding fiscal year and the remaining 40%, a decrease from 50%, will be deposited into the budget stabilization fund. The fiscal year 2009 base is calculated by multiplying \$3,051,500,000 by 1.015 and then multiplying the product by the United States Consumer Price Index for the fiscal year 2009 and then dividing the product by the United States Consumer Price Index for the fiscal year 2007.

For the 2010 fiscal year and each fiscal year after 2010, if the net cash payments exceed the fiscal year base, 60% of the excess, an increase from 50%, will be refunded to taxpayers in the succeeding fiscal year and the remaining 40%, a decrease from 50%, will be deposited into the budget stabilization fund.

The fiscal year base is calculated by multiplying the fiscal year base for the preceding fiscal year by 1.0075 and then multiplying the product by the United States Consumer Price Index for the fiscal year and then dividing the product by the United States Consumer Price Index for the immediately preceding fiscal year.

If the revenue limit is exceeded by less than \$5 million, all of the excess will be credited to the Budget Stabilization Fund.

For the 2008 fiscal year, the refund available, because the MBT exceeds the revenue limits, shall be applied pro rata to the taxpayers that made positive net cash payments during the fiscal year. The taxpayer's pro rata share shall be the total amount to be refunded multiplied by a fraction the numerator of which is the positive net payments made by the taxpayer during the fiscal year and the denominator of which is the sum of the positive net cash payments made by all taxpayers during the fiscal year.

For each fiscal year after the 2008 fiscal year, the refund available shall be applied pro rata to the taxpayers that claimed 1 or more of the credits under Section 403 or 405 (compensation credit, investment tax credit, research and development credit) during the immediately preceding fiscal year. The taxpayer's pro rata share shall be the total amount to be refunded multiplied by a fraction the numerator of which is the credits claimed under Sections 403 and 405 by the taxpayer during the immediately preceding fiscal year and the denominator of which is the sum of the credits claimed under Sections 403 and 405 by all taxpayers during the immediately preceding fiscal year.

The "United States Consumer Price Index means the United States Consumer Price Index for all urban consumers as defined and reported by the United States Department of Labor, Bureau of Labor Statistics.

Please stay tuned for more news and follow the [MichiganStateAndLocalTax Blog](#) for information as it becomes available.

If you have questions please feel free to contact me. I would be happy to be of assistance.

Sincerely,

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