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SFA



BILL ANALYSIS

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Senate Bill 1422 (as introduced 9-18-02)
Sponsor: Senator Joanne G. Emmons
Committee: Finance

Date Completed: 11-12-02

CONTENT

The bill would amend the Single Business Tax Act to exclude from a taxpayer's gross receipts amounts received from the sale of certain securities; and to increase the investment tax credit for taxpayers with adjusted gross receipts of \$5 million or less.

Securities

The Act provides for a gross receipts reduction, if a taxpayer's adjusted tax base exceeds 50% of the sum of the taxpayer's gross receipts plus certain adjustments; at the taxpayer's option, the adjusted tax base may be reduced by that excess. Also, a taxpayer does not have to file an SBT return if the taxpayer's gross receipts, apportioned or allocated as provided in the Act, are less than \$250,000.

"Gross receipts" means the entire amount received by the taxpayer from any activity whether in intrastate, interstate, or foreign commerce carried on for direct or indirect gain, benefit, or advantage to the taxpayer or to others, except for certain amounts specified in the Act. The bill further would exclude amounts received from the sale of securities, including stock, short-term bonds, and notes, in the course of the management of a taxpayer's operating cash accounts.

Investment Tax Credit

Under the Act, a taxpayer may claim an investment tax credit (ITC) for a percentage of the costs paid or accrued in a taxable year for tangible assets physically located in Michigan. Essentially, the credit equals a percentage of the amount a firm invests in tangible assets in Michigan, for a tax year beginning after December 31, 1999; for subsequent tax years the percentage will be reduced each year the tax rate is reduced. (The SBT rate is 1.9% for the 2002 tax year, and is scheduled to be reduced by .1% each January 1 (if there is a balance of at least \$250 million in the Budget Stabilization Fund).)

For taxpayers with adjusted gross receipts of over \$5 million, the ITC is calculated as follows:

$$\frac{(\text{Current Year Tax Rate} \times .85\%)}{2.3\%} \times ([A+B+C] - [D+E+F])$$

Under the formula, A, B, and C represent the costs paid or accrued in a taxable year for tangible assets and mobile tangible assets as provided in the Act; D, E, and F represent the gross proceeds of the sale or other disposition of assets A, B, and C, and the transfer out of State of those assets that are not mobile tangible assets.

The formula is modified for taxpayers with adjusted gross receipts of \$5 million or less. Currently, for taxpayers with adjusted gross receipts over \$1 million but not more than \$2.5 million, the multiplier of .85% is replaced with 1.5% (thus increasing the credit). For taxpayers with adjusted gross receipts over \$2.5 million but not more than \$5 million, the multiplier is 1.0%. The bill would increase the 1.5% multiplier to 1.75%, and the 1.0% to 1.25%.

(For purposes of the ITC calculation, "adjusted gross receipts" are gross receipts apportioned or allocated to Michigan with the apportionment fraction calculated under the Act; plus the gross proceeds or benefits derived from the sale or disposition of assets that had previously been claimed as a deduction as provided in the Act; plus the gross proceeds of the sale or other disposition of tangible assets and mobile tangible assets obtained after 1999, and assets purchased or acquired after 1996 that were transferred out of the State. An affiliated group, a controlled group of corporations, or an entity under common control must determine adjusted gross receipts, for purposes of the ITC, on a consolidated basis.)

MCL 208.7 & 208.35a

Legislative Analyst: George Towne

FISCAL IMPACT

The bill would reduce single business tax (SBT) revenues by an unknown and possibly significant amount.

No information is available on the amount of securities sold in the course of businesses managing their operating cash. In 1999, U.S. corporations reported cash assets at year-end of \$1.6 trillion, compared to \$1.4 trillion in holdings of U.S. government obligations, \$957 billion in tax-exempt securities, \$15.8 billion in "other investments," \$2.6 trillion in "other current assets" and \$2.1 trillion in "other assets." Assuming that: 1) the overwhelming majority of these non-cash assets are not held for the purpose of managing operating cash, a term the bill does not define, 2) in the management of operating cash corporations sell during the course of the year securities valued at an average of 80% of operating cash, and 3) that Michigan activity represents approximately 3.5% of the U.S. total, approximately \$44.7 billion of securities would potentially be affected by the bill.

In 1999, approximately 11.9% of SBT filers calculated their tax liability using a method that was affected by the level of gross receipts. The reduction in liability afforded by these calculations totaled \$250.1 million, or approximately 10.6% of total SBT revenues. Assuming the securities affected by the bill are spread uniformly across all taxpayers, regardless of how they calculate their SBT liability, approximately \$5.3 billion in gross receipts would actually be involved in computing tax liabilities under the bill. If this \$5.3 billion were excluded from the gross receipts calculation, it would reduce revenues by approximately \$50.4 million. The estimate is very sensitive to the share of cash which is rotated through purchases of securities and there is no reliable data regarding that share. For example, if the share were 40%, the bill would reduce revenues by \$25.2 million. Theoretically, the average share could also exceed 100%, although that is unlikely because many smaller firms will not manage operating cash through the use of securities.

The actual impact of the exclusion of these securities could be slightly greater than the amount estimated above for three reasons: 1) lowering gross receipts for firms will allow more firms to qualify for small business credits and/or file under the income tax method, 2) lowering gross receipts will increase the number of taxpayers that find it advantageous to file using a gross receipts method, and 3) the data above only reflects information on corporations, while the SBT taxes a broader array of businesses, including sole proprietorships, partnerships, S-corporations, and other firms not required to report information on the U.S. corporate income tax return.

No information is currently available regarding the effect of the changes in the investment tax credit on revenues, although increasing the multiplier, and therefore the credit, would reduce General Fund revenues.

Fiscal Analyst: David Zin

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.