

CITIZENS RESEARCH COUNCIL OF MICHIGAN

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THE SINGLE BUSINESS TAX IN MICHIGAN

The Capital Acquisition Deduction

Background

The single business tax (SBT) was enacted in 1975. It is a modified “value added” tax on the use by a business of labor and capital to increase the market value of a product or service. The SBT is imposed upon all taxpayers having business activity in Michigan. The base of the SBT is the sum of all compensation paid, profit, interest paid, and depreciation, minus a deduction for capital acquisitions and certain other adjustments including a labor intensity deduction.

The “Single” Business Tax is so named because it replaced with a single tax eight different business taxes then imposed on business including the corporate income, franchise and business intangibles taxes and the general property tax on inventories. The SBT was designed to simplify the tax structure, achieve neutrality among different forms of business organization, encourage capital investment in Michigan, and yield the same amount of revenue as the eight taxes it replaced.

The single business tax has been a productive and stable source of state tax revenue. In 1990 the SBT yielded \$1.8 billion, an increase of 124% since the first full year of collection in 1977. The SBT is the third largest state tax (after income and sales) and accounts for one-sixth of total state tax revenues. The SBT has been a reasonably stable source of revenue over time, representing between 14.2% and 17.8% of total state tax revenue. In 1990, the SBT was 16.2% of total state tax revenue, which is about the average for the 14-year period.

Issues

In the 1991 legislative session, major changes were made in the SBT in response to Michigan Court of Claims and Court of Appeals rulings on the apportionment of the capital acquisition deduction (CAD). The courts ruled that the existing method of apportioning the capital acquisition deduction for real and personal property.. which was different from the method of apportioning the SBT base, was unconstitutional because it discriminated against interstate commerce. The Court of Claims eliminated the CAD completely, which would have increased state revenues by about \$500 million, while the Court of Appeals eliminated only the apportionment of the deduction, allowing an unapportioned capital acquisition deduction from the apportioned tax base of multi-state businesses. This would have reduced state revenues by about \$450 million. Apportionment provisions affect only multi-state business operations and do not apply to taxpayers whose business activity is entirely in Michigan.

Public Act 77 of 1991 resolved the apportionment issue by adopting a new apportionment method increasing the weight of the sales factor which would apply to both the capital acquisition deduction and the SBT base. Both the CAD and the SBT would be apportioned as follows:

1990	33% property, 33% payroll, 33% sales
1991 and 1992	30% property, 30% payroll, 40% sales
1993 and after	25% property, 25% payroll, 50% sales

There are some fall-back provisions in P.A. 77 in the event the Courts do not concur with the resolution of this issue. In addition to the apportionment changes, P.A. 77 also increases the filing threshold for small businesses. Businesses with gross receipts of \$40,000 or less do not have to file under current law. This will increase to \$60,000 for 1991 and to \$100,000 for 1992 and thereafter. This will eliminate the tax on an estimated 18,000 small businesses.

Even if the Courts concur in the apportionment formula changes, the capital acquisition deduction issue is not completely settled. Initiative petitions for a statute are being circulated to place on the November 1992 ballot a House Democratic proposal to provide for homestead property tax relief and finance it by repealing the capital acquisition deduction and industrial property tax abatements (existing as well as future abatements would be repealed). This would increase business taxes by \$700-\$750 million annually.

Businesses in Michigan already bear a very high single business tax burden compared to corporate income taxes in other states. The U.S. Bureau of the Census, which classified the SBT as a corporate income tax, reports that in 1989 the SBT in Michigan was \$100 per capita or 90% higher than the U. S. average. This amounts to a \$900 million excess business tax burden compared to other states. The U.S. Advisory Commission on Intergovernmental Relations reports that the Michigan taxes on "corporate net income and net worth" which includes the SBT were second highest among the 50 states in 1988. Further increase in business taxes by repealing the capital acquisition deduction would make Michigan even less competitive with other states.