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Small Business Taxation in Michigan

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About Anderson Economic Group, LLC

- Anderson Economic Group is a research and consulting firm specializing in economics, public policy, industry research, and business valuation with offices in East Lansing, Michigan; Chicago, Illinois; and Istanbul, Turkey.
- Clients include universities, trade associations, private companies, non-profit associations, and state and local governments.
- We have performed studies on business taxes and their effects in Michigan, Pennsylvania, Kentucky, and other states.
- Since 2006, we have published an annual study on the business tax burden in all 50 states using an original methodology.



METHODOLOGY

Our approach to measuring the state and local tax burden is to estimate the total amount of state and local tax paid by businesses in each state and divide it by a measure of business operating margin.

We used over a dozen state and national sources to collect this information on 10 different categories of taxes, including property, income, sales, excise, license, severance, and other taxes.

All data that we use is publicly available. See our annual Tax Burden Study for a full description of our methodology.

FINDINGS

- Michigan state and local governments collected \$14.3 billion in taxes from businesses in 2013 (out of \$36.8 billion total taxes collected).
- These taxes represented 8.9% of firms' pre-tax operating surplus, placing Michigan 23rd among all states in business tax burden.
- This was an estimated decline in tax collections from businesses of nearly \$1 billion from the previous year.
- This decline in taxes paid by business is primarily the result of the elimination of the gross receipts tax due to repeal of the Michigan Business Tax, and a decrease in property taxes and general sales taxes paid.

FINDINGS

- A majority of businesses are organized as sole proprietorships, partnerships, or S corporations, and the owners of these companies pay taxes on net profits through the individual income tax. Individual income taxes on so-called “pass-through” income from these businesses increased to \$800 million in 2013.
- Certain forms of taxes disproportionately affect small businesses relative to other firms, including personal income tax on pass-through income, general sales taxes, and license fees.

BUSINESS TAXES IN MICHIGAN

Businesses in Michigan pay many different taxes at the state and local level.

We have identified 10 types of state and local taxes paid by business totaling over \$14.3 billion combined in 2013, as shown in Table 1 on the next slide.

This represented nearly two-fifths of the \$36.8 billion of total taxes collected by state and local governments in Michigan that year.

BUSINESS TAXES IN MICHIGAN

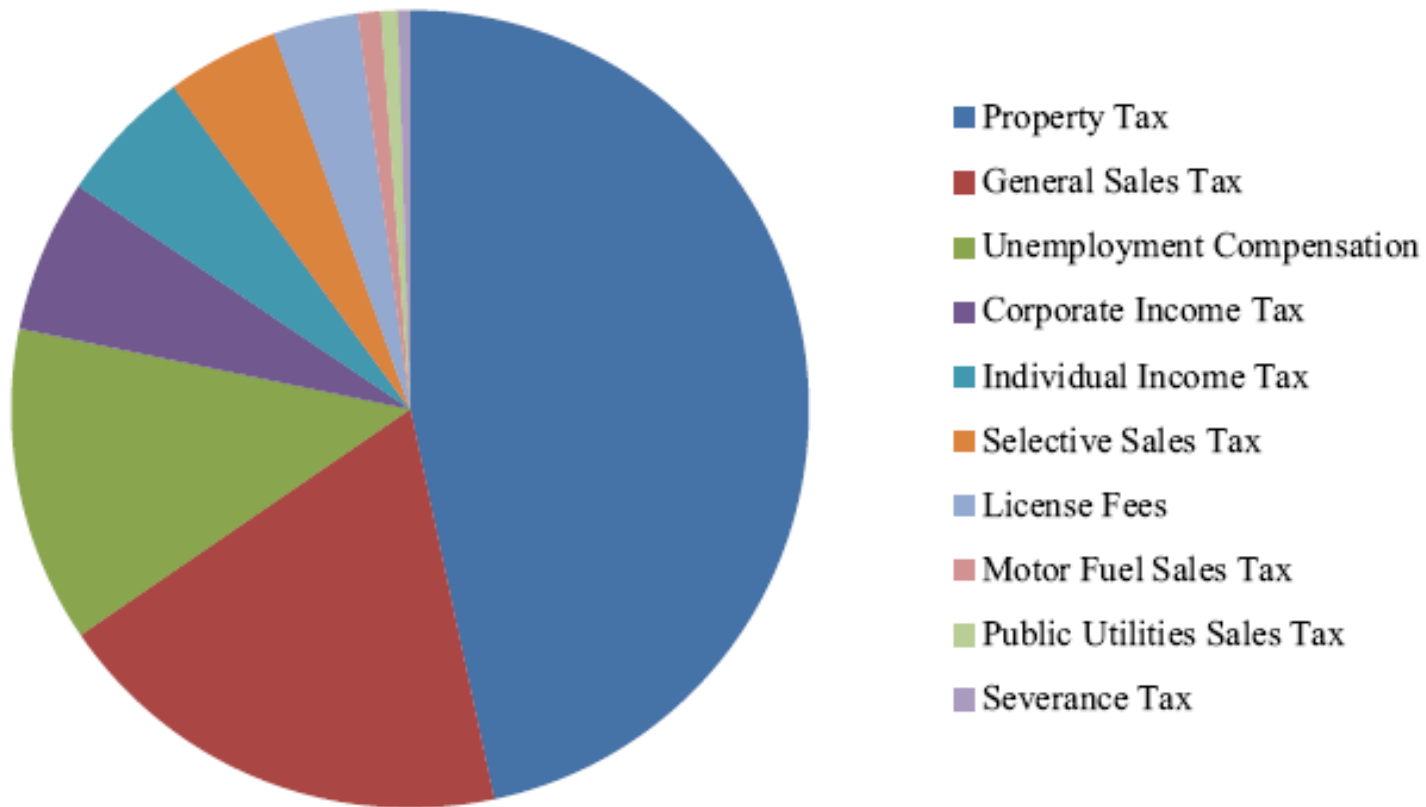
TABLE 1. Total State and Local Taxes Paid by Michigan Businesses, 2012 and 2013

Type of Tax	2013 Taxes Paid (millions of \$)	% of Total	2012 Taxes Paid (millions of \$)
Property tax	\$6,787	47.4%	\$7,259
General sales tax	\$2,494	17.4%	\$2,735
Unemployment compensation tax	\$1,864	13.0%	\$1,924
Corporate income and gross receipts tax	\$901	6.3%	\$1,322
Individual income tax on pass-thru business income	\$801	5.6%	\$677
Selective sales tax	\$661	4.6%	\$621
License Fees	\$499	3.5%	\$460
Motor fuel sales tax	\$136	1.0%	\$122
Public utilities sales tax	\$100	0.7%	\$96
Severance tax	\$70	0.5%	\$64
Total State and Local Taxes Paid by Businesses	\$14,312	100%	\$15,280

Source: Anderson Economic Group analysis and estimates, using base data from U.S. Census of Governments State and Local Finance Survey and other federal and state sources.

BUSINESS TAXES IN MICHIGAN

FIGURE 1. Proportion of Michigan Business Taxes by Type



Source: Anderson Economic Group analysis and estimates, using data from U.S. Census of Governments State and Local Finance Survey and other sources.

IMPACT ON SMALL BUSINESS

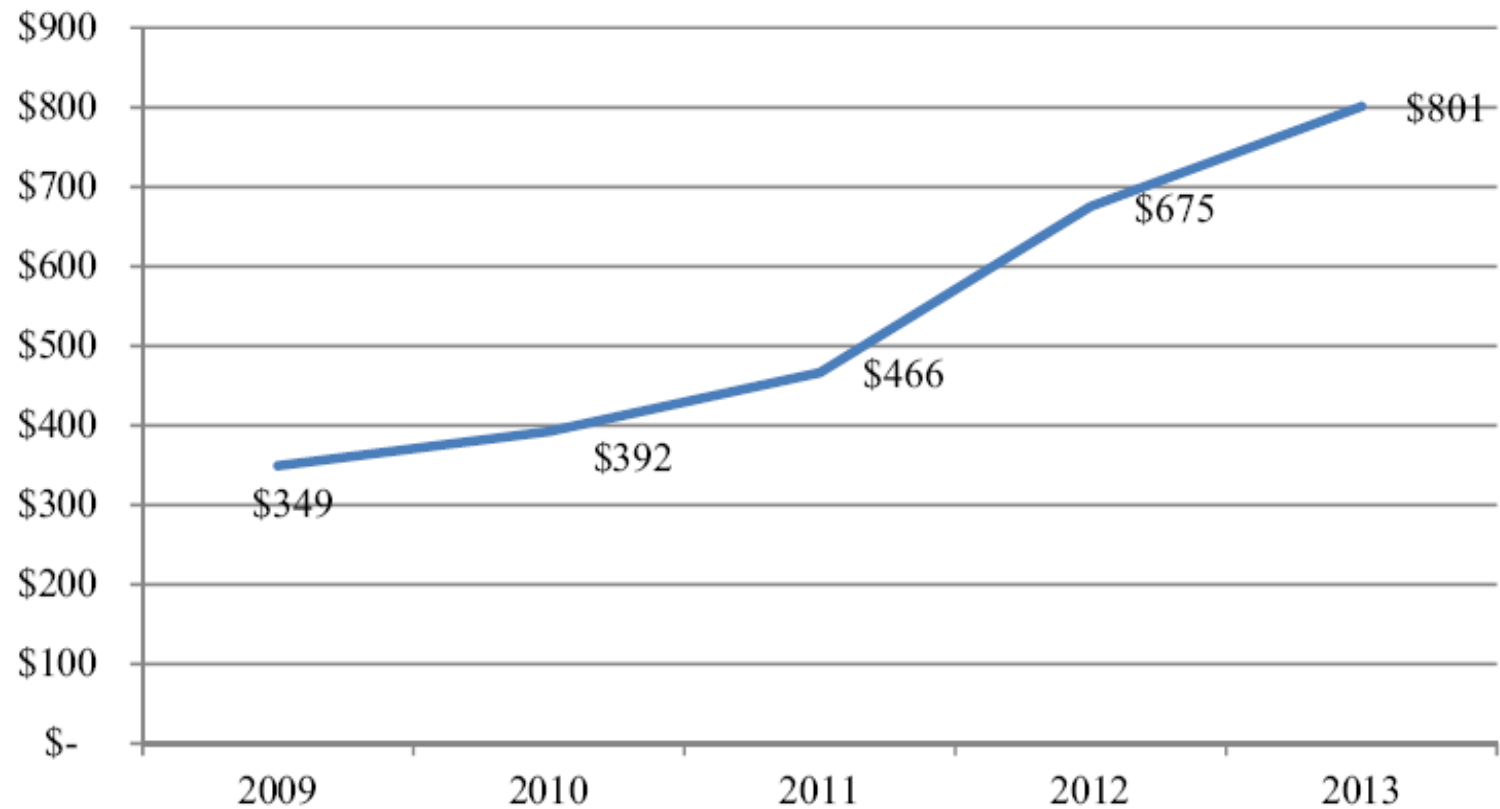
Clearly, not all taxes are distributed equally among Michigan businesses.

The individual income tax that is assessed on pass-through business income is predominantly paid by small business owners, particularly sole proprietors, partnerships, LLCs and S Corporations which are not subject to the corporate income tax.

Profit returned to owners is treated as if it were regular individual income by the state. As Michigan has recovered from the recent recession, individual income tax revenues from net business income have risen considerably, more than doubling from under \$400 million to approximately \$800 million in 2013. As shown in Figure 2 on the next slide.

IMPACT ON SMALL BUSINESS

FIGURE 2. Individual Income Tax on Pass-through Business Income, FY 2009 to FY 2013



Source: Anderson Economic Group analysis and estimates, using data from U.S. Census of Governments State and Local Finance Survey and other sources.

IMPACT ON SMALL BUSINESS

- The corporate income tax is assessed on C Corporations alone, relatively few of which are small businesses.
- Taxes likely to disproportionately effect small businesses include the individual income tax (described earlier), property tax, sales tax, and licensing fees.
- Small businesses are less likely to receive incentives that reduce their property tax and sales tax burden.
- General sales taxes on major purchases for equipment and other items are exempted for larger enterprises more often than for small enterprises due to the industry concentration of small businesses, the administrative burden of receiving exemptions, and other factors.

IMPACT ON SMALL BUSINESS

Type of Tax	Total Taxes Paid (millions of \$)
Property tax	\$6,787.0
General sales tax	\$2,737.0
Individual income tax on pass-thru business income	\$801.1
Selective sales tax	\$661.1
License fees	\$499.0
Total	\$11,485.2
<i>Other State and Local Taxes Paid by Businesses</i>	<i>\$2,949.5</i>

Source: Anderson Economic Group analysis and estimates, using base data from U.S. Census of Governments State and Local Finance Survey and other federal and state sources.

Note: These totals include payments by both small and large businesses in Michigan. We show here the total amounts paid by business for the types of taxes that tend to particularly impact small businesses.

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OBSERVATIONS

- 2013 Revenue from the Corporate Income Tax and MBT = \$901 Million
- 2013 Revenue from the Small Business Income Tax = \$801 Million
- Extrapolation of 2013 data to 2014 shows revenue Small Business Income Tax = \$800 Million (about the same)
- 2014 data from House Fiscal Agency shows Revenue from the Corporate Income Tax and MBT = \$183 Million – 328 Million

Consensus Revenue Estimating Conference Overview

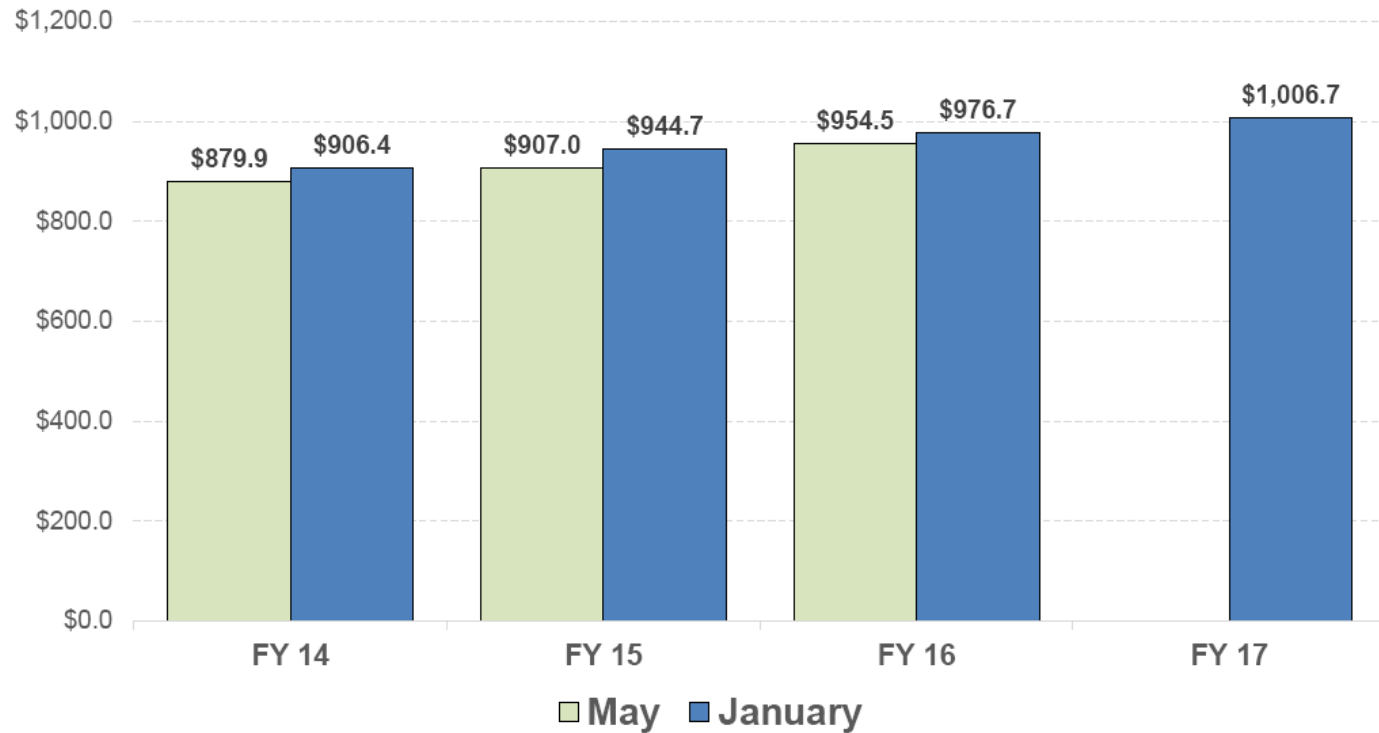
**Mary Ann Cleary, Director
House Fiscal Agency**

**House Appropriations Committee
January 28, 2015**



Corporate Income Tax (CIT)

(Dollars in Millions)



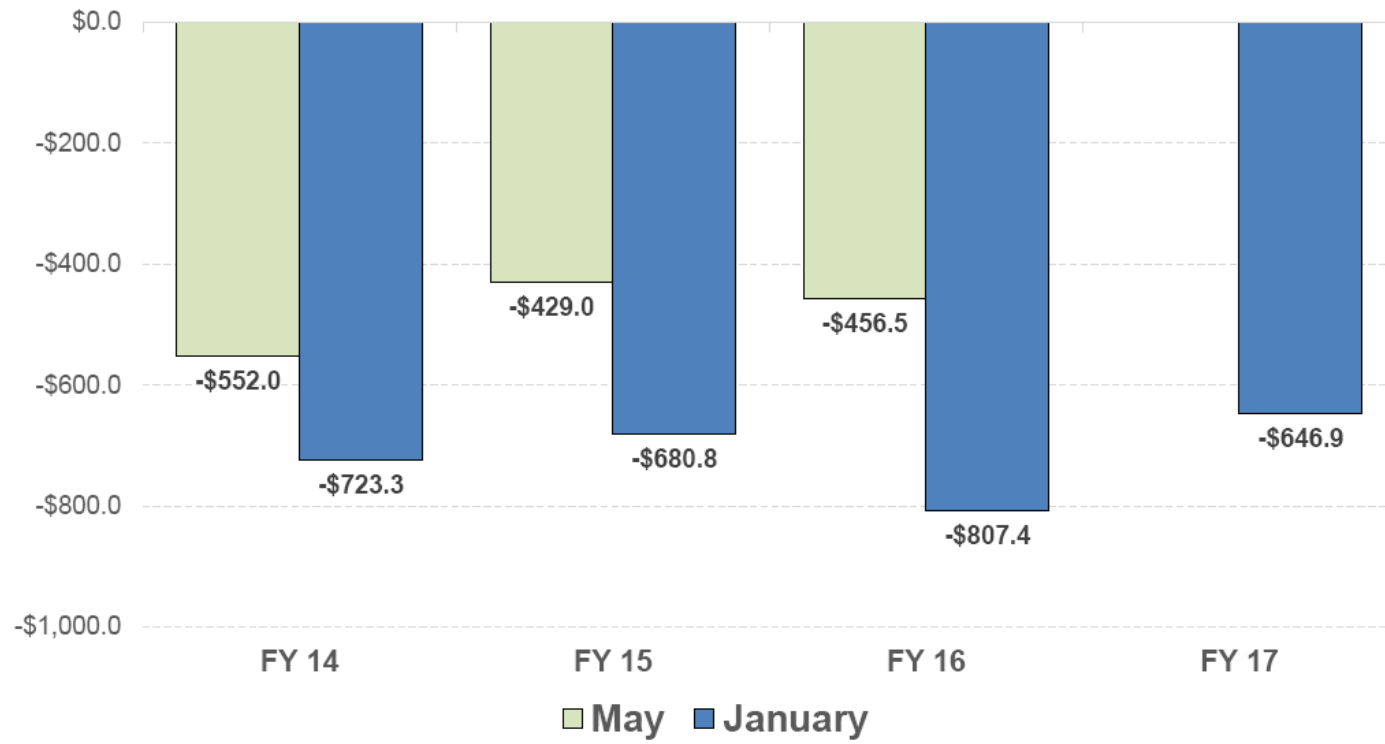
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House Fiscal Agency

1/28/2015

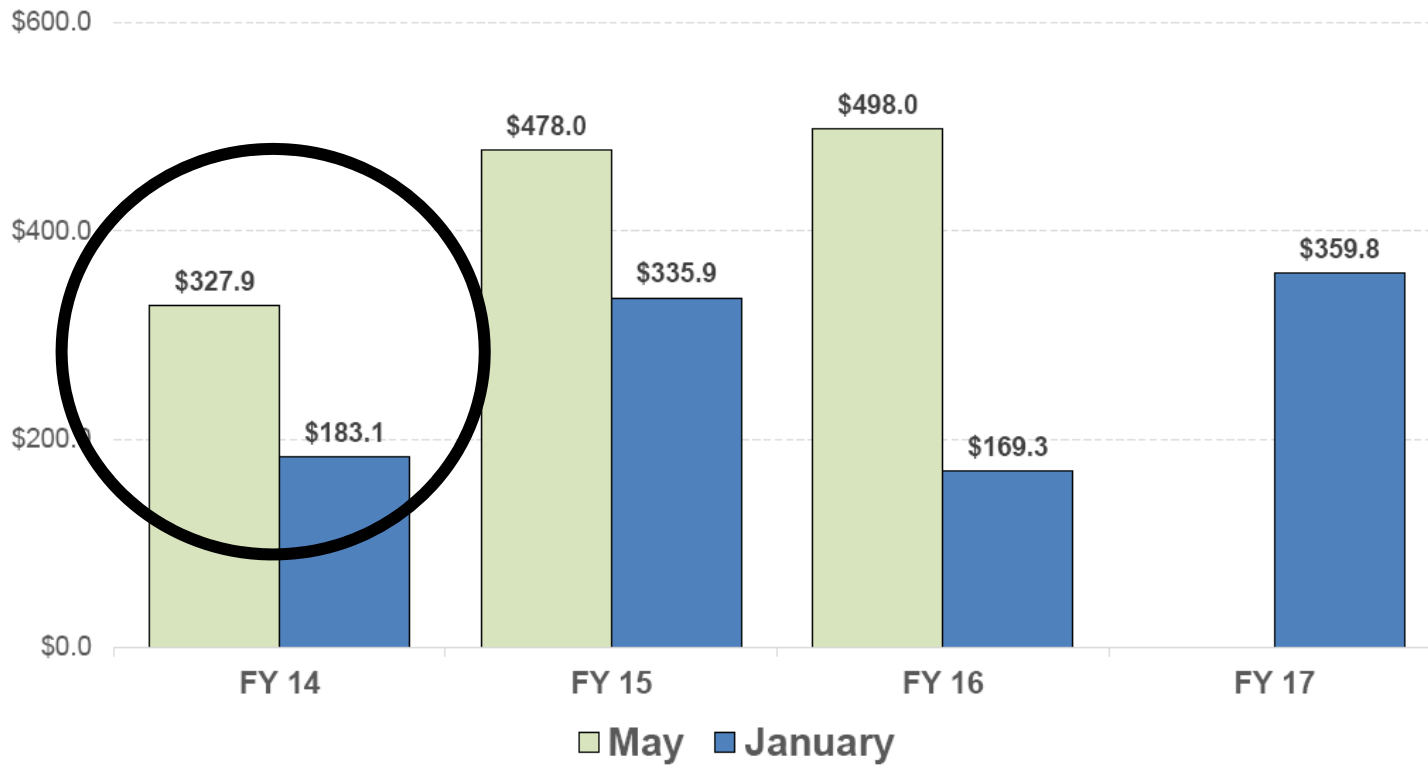
Michigan Business Tax (MBT)

(Dollars in Millions)



Net Combined Business Taxes (CIT / MBT)

(Dollars in Millions)

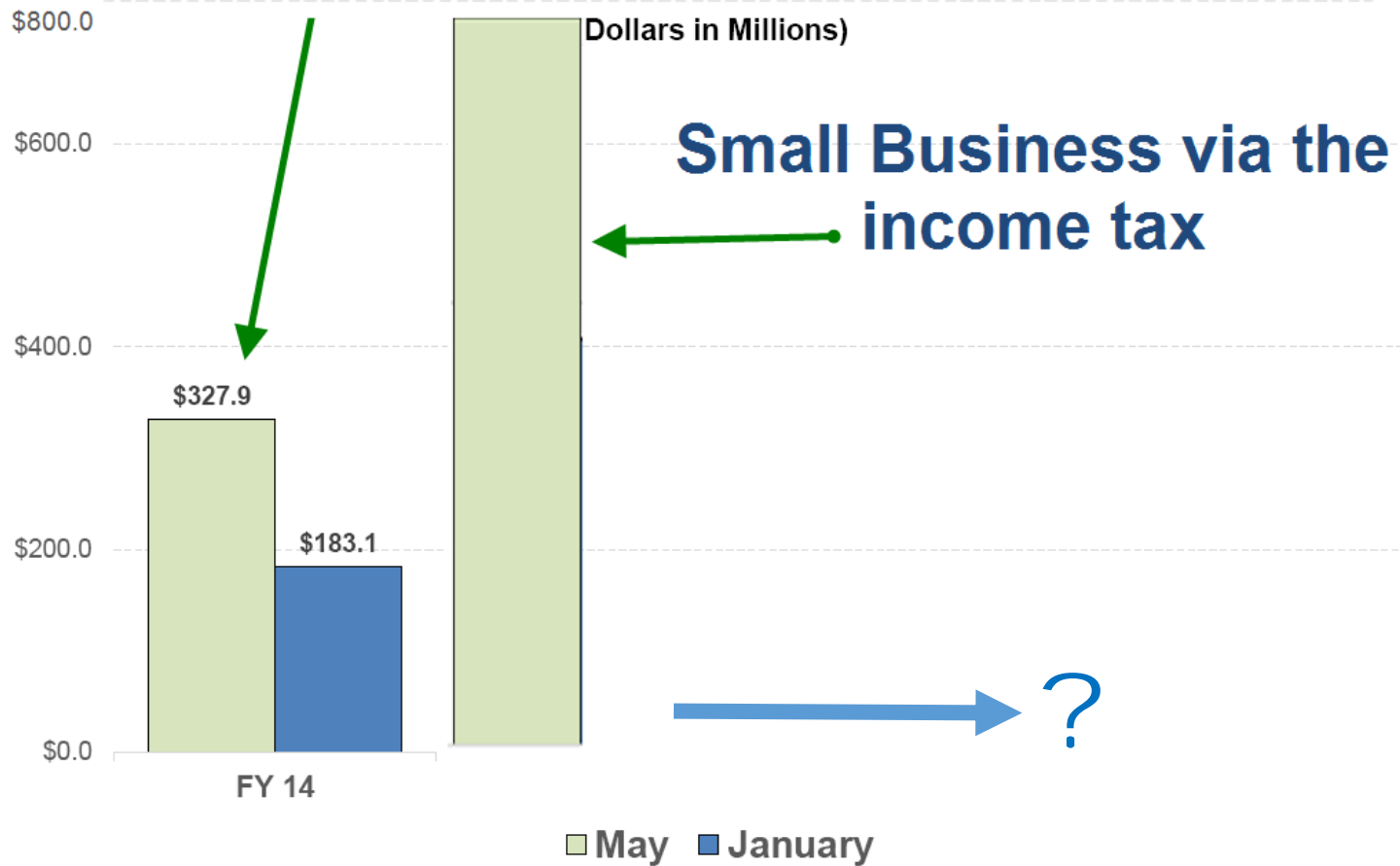


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↑ Net Combined Business Taxes (CIT / MBT)





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CONCLUSIONS

During the recent gubernatorial debate, candidate Mark Schauer hinted at the fact that there are some 95,000 businesses in the state not now paying the Corporate Income Tax. In a follow up interview with the Detroit Free Press Editorial Board, Schauer repeated his concern that 95,000 businesses are not paying the Corporate Income Tax.

Recently, former House Fiscal Agency Analyst, Mitch Bean suggested that lawmakers could grab a quick \$1 billion in revenue by “expanding the base and lowering the rate” in other words, lasso in those 95,000 businesses “not paying taxes” into the Corporate Income Tax.

Apparently, a small business only pays taxes if they pay twice on the same income, not once. The reason they are not paying the Corporate Income Tax is because they already paid their business income taxes with their personal income taxes, and as just illustrated they are paying MORE!



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CONCLUSIONS

If you “broaden the base” (include other than C corps) you have just recreated the Michigan Business Tax – the worst business tax in the nation according to the Tax Foundation.

Lower the rate? If you consider the refundable credits that are now coming home to roost – you have already lowered the rate to something less than what non-C corp small businesses are paying (4.25% on income). You would be lowering the rate for most of the companies in the state that are not paying the effective 6% rate now.

The legislature and the Governor have worked hard to dig Michigan out of the hole it was in just four short years ago. We have finally got it right when it comes to business taxation in this state. It is imperative that you avoid the temptation to go back to the failed business tax policies of the past and squander the progress made.

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