New Michigan Corporate Income Tax

5-25-2011 by *Jay A. Kennedy*, *Scott M. Hancock*

Michigan will have a new corporate income tax structure starting January 1, 2012. The Michigan Legislature passed two bills, House Bill 4361 and House Bill 4362, which Governor Snyder signed today. This new legislation will considerably alter Michigan's business tax system.

Starting next year, the Michigan Business Tax (MBT) will be replaced by a corporate income tax (CIT) that will apply to business entities that are 'C' corporations for federal income tax purposes. A 'C' corporation will be subject to the CIT if it has a physical presence in Michigan, or actively solicits sales in Michigan and has gross receipts of at least $350,000 sourced to Michigan. 'C' corporations with an ownership or beneficial interest in a flow-through entity with Michigan nexus will also be subject to the CIT.

A 'C' corporation will not be required to file a return or pay tax if its apportioned or allocated gross receipts are less than $350,000 or the corporation's tax liability is $100 or less. The CIT retains unitary filing requirements for 'C' corporations under common control.

In general, the CIT tax rate will be 6 percent of a 'C' corporation's federal taxable income, as statutorily adjusted, after allocation or apportionment to Michigan. However, insurance companies will be subject to a tax rate of 1.25 percent of gross direct premiums written on property or risk located or residing in Michigan, and financial institutions will be subject to a tax rate of 0.29 percent of their net capital after allocation or apportionment to Michigan.

The CIT requires 'C' corporations with Michigan and non-Michigan business activities to apportion business income using the ratio of Michigan sales to total sales. Apportioned sales of a unitary business group will include all sales in Michigan of every member of a unitary business group, whether or not a member has Michigan nexus. Non-Michigan 'C' corporations will no longer be able to apportion business activity to Michigan based on property, payroll or any other factors other than sales, as was previously permitted by the Multistate Tax Compact.

The CIT will not continue credits available to taxpayers under the MBT other than the small business alternative tax credit. This credit will allow qualified small businesses to pay tax at a rate of 1.8 percent of adjusted business income instead of 6 percent. This credit will be available to 'C' corporations with gross receipts that do not exceed $20 million, adjusted business income that does not exceed $1.3 million, and officers' and owners' compensation that does not exceed $180,000 per individual. The credit will be subject to phase-out for gross receipts between $19 million and $20 million and officers' and owners' compensation between $160,000 and $180,000 per individual.

A 'C' corporation that has been awarded certain tax credits under the MBT may continue to use those credits for tax years beginning after January 1, 2012, if the corporation elects to pay tax under the MBT. Individuals and business entities not subject to the CIT will also be able to elect to pay tax under the MBT in order to take advantage of previously awarded tax credits. The tax liability for a taxpayer making the election will be the greater of the taxpayer's tax liability under the MBT or the new CIT, less the tax credits. Under certain circumstances, taxpayers will be eligible to receive a refund of tax credits that exceed their tax liability.

If you have questions about the changes or any other tax issue, please contact Jay Kennedy (248.784.5180 or jkennedy@wnj.com), Scott Hancock (616.752.2713 or shancock@wnj.com) or any other member of the Tax Law Group at Warner Norcross & Judd.