

TAX BREAKS AND EXEMPTIONS: WHAT EVERY SMALL BUSINESS SHOULD KNOW

Entrepreneurs and small business owners must pay close attention to the fundamentals of taxation and business costs to participate in a competitive market. Below are some highlights that business owners should review and, as necessary, discuss with a tax preparer, business consultant, or tax attorney. The list is not exhaustive and should only serve as a starting point for understanding business costs.

It is important to note that newly-created Michigan businesses may use Form 518, "Registration for Michigan Taxes," to select and create tax accounts for business taxes, sales taxes, withholding taxes, unemployment insurance taxes, motor fuel taxes and tobacco taxes, as needed. Details about starting and operating a business may be obtained through Michigan's new one-stop online service at www.michigan.gov/business or by phone at 877.766.1779.

MICHIGAN BUSINESS TAX (MBT)

The Michigan Business Tax (MBT) contains several features aimed at reducing the tax burden on small businesses. In implementing this tax in 2008, Michigan made a concerted effort to include provisions that would encourage small business creation and growth. Here are some key provisions:

Filing Threshold

Businesses earning less than \$350,000 in gross receipts are not required to file or pay the MBT.

Phase-In Credit

Businesses with gross receipts between \$350,000 and \$700,000 will phase-in their MBT liability.

Small Business Alternative Tax Credit

The Small Business Alternative Credit's qualifying criteria has been recently expanded to make more business owners eligible. Instead of the MBT's usual calculation, qualified small businesses pay an alternate tax equal to 1.8% of adjusted business income. In order to qualify, the business must meet the following standards:

- Adjusted business income cannot exceed \$1.3 million (indexed to inflation).

- Gross receipts cannot exceed \$20 million and the credit is phased-out between \$19 and \$20 million in gross receipts.
- Officer's/owner's compensation cannot exceed \$180,000 (The credit phase-out range for officer compensation is \$160,000–\$180,000.)

Entrepreneurial Credit

The Michigan Entrepreneurial Credit rewards entrepreneurs that create jobs in Michigan. Businesses that earn less than \$25 million in gross receipts, invest at least \$1.25 million in Michigan and create at least 20 jobs can take a credit against the MBT in 2008, 2009 and 2010. The size of the credit depends on the number of jobs the business creates relative to their current size. This credit could provide some businesses with a 100% reduction in their MBT liability.

Start-Up Credit

This credit targets small, relatively new taxpayers with substantial research and development activity. The credit is equal to the taxpayer's liability for the year. A qualified taxpayer must (1) have fewer than 25 employees; (2) have sales of less than \$1 million; (3) not be publicly traded; (4) have R&D make up at least 15 percent of its expenses; and (5) be in one of the first two years of contribution for unemployment insurance taxes in the immediately preceding seven years.

Details about MBT credits and forms can be located at www.michigan.gov/mbt.

UNEMPLOYMENT INSURANCE

Business may obtain an unemployment insurance tax account with the Michigan Unemployment Insurance Agency (UIA) using the business registration Form 518. For new employers, the tax rate will be 2.7% in the first two years of operation. The taxable wage base per employee is \$9,000 annually. With no layoffs, the new employer rate can drop to 1.7% and 1% in years three and four of operation, respectively. An experience-based rate is implemented in year five of operations and thereafter.

Generally, there are three ways that an “employing unit” in Michigan can become responsible for paying unemployment insurance “contributions” (taxes) to UIA:

1. If the employing unit employs one or more persons in any 20 different calendar weeks (Sunday through Saturday) in a calendar year (January 1 through December 31); *or*
2. If the employing unit pays (or owes payment of) total wages of \$1,000 or more in a calendar year.
3. If the employing unit acquires the organization, trade or business, or 75% or more of the assets of a company that was already an employer liable for the payment of unemployment taxes. Becoming an employer in this way is known as “successorship.”

There are different provisions for employers of domestic and agricultural workers.

For more unemployment insurance information, visit www.michigan.gov/uia.

WORKERS' COMPENSATION INSURANCE

Small businesses may obtain workers' compensation insurance coverage through Michigan insurance agents, available group self-insurance funds, or through the Michigan Placement Facility's Assigned Risk Pool.

All private employers must have workers' compensation coverage if:

1. They regularly employ three or more workers at one time; *or*
2. During the preceding 52 weeks, they have regularly employed at least one worker for 35 hours or more per week for 13 weeks or longer.

All public employers must have coverage; any other employers can voluntarily choose to buy workers' compensation insurance coverage. Michigan has special provisions that apply to contractors, subcontractors and sole proprietors.

Limited exclusions from required workers' compensation insurance coverage are available to qualified employers. To inquire about exclusions, companies should contact the agency's Compliance & Employer Records Division at 517.322.1195.

For more workers' compensation information, including a listing of group self-insurance funds, visit www.michigan.gov/wca. Information about the

Michigan Placement Facility's Assigned Risk Pool is located at www.caom.com.

SALES TAX

Companies selling tangible property to end users or consumers can get a sales tax license using the Form 518, “Registration for Michigan Business Taxes.”

Claims for a sales tax exemption should not be directed to the Michigan Department of Treasury. Instead, the sales tax exemption should be claimed from the seller of the product. The seller should be provided with a completed and signed Form 3372, which can be good for up to four years as a blanket exemption claim or for one-time purchases. The form establishes under which provision the buyer is claiming the exemption. Details on the eligibility standards for the exemption provisions can be found in the Michigan Department of Treasury **Revenue Administrative Bulletin 2002-15**.

General questions about the exemption may be obtained from the Sales, Use and Withholding Technical Unit by calling 517.636.4730 and selecting prompt #2 (staff will come on the line if no account number is entered).

Sales tax information and revenue administrative bulletins may be obtained at www.michigan.gov/taxes.

PROPERTY TAX

Under recent tax reforms, commercial personal property is exempt from 12 of 24 education mills, while purchased industrial personal property is exempt from all 24 education mills. (Full exemptions will not apply in any of the 28 “Hold Harmless” school districts located in the state.) Local property tax assessors can answer questions about these exemptions and about industrial and commercial property classifications.

Firms also receive a 35% refundable MBT credit for remaining industrial personal property taxes paid. On average, these tax reductions provide a 65% cut on purchased industrial personal property taxes and a 23% reduction in commercial personal property taxes.

Eligibility criteria vary among the available property tax abatement programs, which are administered at the local government level. Company officials should contact their local economic development organizations to discuss property tax abatement programs.

Available programs include:

Plant Rehabilitation and Industrial Development District

Public Act 198 (P.A. 198) provides property tax abatements to industrial processors, high-technology activity companies, research and development laboratories and large communication centers, which can reduce certain property taxes by up to 50% through the Industrial Facilities Tax. A P.A. 198 abatement is negotiated at the local level and is available for up to 12 years. Investment made within the negotiated time will be eligible for the abatement. Once the abatement is granted, businesses are required to pay taxes under an Industrial Facilities Exemption (IFE).

New Personal Property Exemption

Public Act 328 of 1998 (P.A. 328) allows distressed communities, county seats, certain border county communities and businesses authorized under the Michigan Economic Growth Authority (MEGA) to abate all new personal property taxes in order to spur economic development. The entire millage rate is abated under P.A. 328. All new personal property installed by an eligible business, after local approval, is 100% exempt from personal property taxes for a specified period determined by the local unit of government. The exemption is not project-specific and would exempt all new personal property installed by the business for the time specified by the local unit of government.

Obsolete Property Exemption

Public Act 146 of 2000 provides for a tax incentive to encourage the redevelopment of obsolete buildings into commercial or commercial housing. The tax incentive is designed to assist in the redevelopment of older buildings, in which a facility is contaminated, blighted or functionally obsolete. The taxable value on a facility is frozen for up to 12 years. By freezing the taxable value, a business can significantly improve a building without increasing the property taxes on the building.

Commercial Rehabilitation Act

Public Act 210 of 2005 provides a property tax abatement for commercial real property that is 15 years or older. The primary purpose and use is the operation of a commercial business enterprise or multi-family residential use. The commercial rehabilitation tax freezes the taxable value of that building and only levies specific taxes on the new investments.

Renaissance Zones

Renaissance Zones[®] are regions of the state set aside as virtually tax-free for any business or resident that locates in one of the zones. Taxes that are due are those mandated by the federal government, local bond obligations, school sinking fund or special assessments. In all cases, the tax relief will be phased out in 25% increments over the last three years of the zone.

ADDITIONAL SERVICES AND PROGRAMS

SBTDC Network

Michigan has a network of Small Business & Technology Development Centers (SBTDCs) around the state to assist entrepreneurs and small business owners in establishing and growing a business. The SBTDC network provides direct counseling, training and research for people with new and existing small businesses. Information about the network can be found at www.gvsu.edu/misbt/dc or by calling 616.331.7480.

Capital Access Program

Over 50 Michigan financial institutions participate in the Capital Access Program (CAP). Participating banks offer CAP loans directly to companies that need credit enhancement, including long- or short-term loans, term loans or lines of credit. Eligible companies must contact participating lenders directly, as the CAP loans are private transactions between the bank and the borrower. Eligible for-profit firms must have less than 250 employees or less than \$6 million in gross annual sales. The maximum loan amount is \$5 million.

Guide to Starting a Small Business

The *Guide to Starting a Small Business* contains information on a variety of small business topics, including information on business plans, financing and managing your business. The guide may be found online at www.TheMEDC.org/startupguide.