



TAX ON SERVICES?

Michigan Mulls Major Sales Tax Shift

QUICK TAKE

- Business leaders, academics, economists, and the state's Governor want to restructure Michigan's sales tax to include both goods and services
- The proposal would make Michigan a stronger contender in attracting and keeping business
- The new plan would modernize our tax structure, but implementation would be a major undertaking



An innovative proposal that would fundamentally restructure Michigan's sales tax is on the State's legislative agenda. The plan? Expand the scope of sales tax to include services as well as goods.

Currently, Michigan taxes only a few services—telecommunications being one prime example. But economists point out that a conventional sales tax covering only goods is increasingly out of synch with our modern economy, where the service sector now represents 80% of all employment. Since services tend to be purchased to a greater degree by higher income consumers, economists say the proposed service tax would be fairer.

BUSINESS, GOVERNOR BOTH ISSUE PLANS

In January, Business Leaders for Michigan (a group composed of the state's top execs and academics formed as part of the Michigan Turnaround Plan) issued a proposal calling for the imposition of a sales/use tax on all services except for business-to-business transactions, health care, education, and housing.

Their plan recommends an across-the-board 5.5% tax rate (a half percent cut from the current rate, which applies to goods) on all but excluded purchases. Revenues would be dedicated to the repeal of the Michigan Business Tax (MBT) surcharge (generally equal to almost 22% of the tax before credits), as well as a reduction in the MBT gross receipts tax rate, from 0.8% to 0.45%.

In February, Michigan Governor Jennifer Granholm proposed a similar expansion of the service tax as part of her 2010-2011 budget message. The Governor's proposal would establish the same tax rates and

essentially the same exemptions as the Business Leaders' plan, but would phase out the repeal of the MBT surcharge over two years and lower the gross receipts tax rate to 0.6% over three years. The proposal would apply the additional revenue generated (estimated at \$533M in 2011 and \$330M in 2012) to the state's budget.

BEEN THERE, DONE THAT?

What's that, you say? Didn't Michigan go down that road before? Not exactly.

Late in 2007, the State Legislature put forth a similar sales/service use tax to a number of enumerated services. But, because of ambiguities in definitions of services to be taxed, the plan was repealed on the eve of its effective date and replaced with the controversial MBT surcharge.

It may seem like we've gone full circle—but this new proposal differs in an important way. It would tax all services with specified exemptions, rather than only certain listed services. Another key difference: the plan comes not from the government sector, but from the private sector—giving it credibility and greater acceptance.

HOW WOULD MICHIGAN'S ECONOMY BE IMPACTED?

If enacted, the new tax structure would make Michigan far more competitive in attracting business—moving it closer to the stated goal of achieving "Top 10" status in terms of business tax burden. It would also move Michigan to the head of the list in deriving the largest amount of tax revenue from services.

SOME ISSUES REMAIN

If this sweeping proposal goes forward, it will be important to provide substantial lead time to allow service businesses to gear up, and let taxpayers prepare to comply. Questions will likely arise about extending input credit for taxable items used in rendering taxable services to avoid double taxation. And defining the scope of exempt services could create speed bumps. It's certain that tax practitioners and the business community will need to participate in shaping legislation of this magnitude.

But if it does happen, Michigan will deserve recognition for outside-the-box thinking when it comes to tax policy.

TWO LEADING MICHIGAN TAX LAWYERS JOIN THE FIRM

Miller Canfield has expanded its state and local tax expertise with the recent addition of two seasoned tax lawyers. Jack Van Coevering and Gregory A. Nowak bring a wealth of experience in taxation, tax litigation, and dispute resolution.

Nowak—who is a CPA—began his legal career at our firm before joining PricewaterhouseCoopers, where he was a partner and leader of the tax consulting practice. Over the years, he has been widely recognized for his contributions to the tax profession at both state and regional levels, and was instrumental in developing tax policy during the enactment of the Michigan Business Tax and repeal of the then proposed service tax.

Van Coevering serves as senior counsel in our Grand Rapids and Lansing offices, where he focuses on state and local tax litigation and dispute resolution.

With 15 years of tax experience, Van Coevering also served as Chief Judge of Michigan's Tax Tribunal, led the legal division and administrative hearings division of the Michigan Department of Treasury, and was assistant attorney general in the Revenue Division, where he litigated numerous state and local tax cases.



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