GROSS RECEIPTS TAXES

What is a Gross Receipts (Hawaii - Gross Excise) Tax:

It is a tax imposed for the privilege of engaging in business in the state that levies the tax. The tax is levied on gross income derived from a business activity. This includes income from the sale of tangible personal property at both the wholesale and retail level, sale of services, contracting, commissions, interest, lease or rental activities and more. It is a business tax not a consumption tax like the sales tax, though it can be passed on to consumers. The tax is imposed on the business rather than the consumer. It is considered to be an expense which businesses incur in the normal course of doing business.

How does the tax compare to a sales tax:

Exhibit A is a comparison prepared by the New Mexico State Tax Research Department that compares the gross receipts tax to a sales tax. Since the comparison primarily applies to the New Mexico, Exhibit B contains a table that compares the Hawaii version of the tax to a sales tax.

Comparison of the New Mexico Gross Receipts Tax and the Hawaii Gross Excise Tax:

	New Mexico	Hawaii
Imposition	Tax is imposed on persons engaged in business for the privilege of doing business in New Mexico	Tax is imposed on persons engaged in business for the privilege of doing business in Hawaii
How Levied	Tax is levied against the gross receipts of a business minus allowable deductions/exemptions.	Tax is levied against the gross receipts of a business minus allowable deductions/exemptions.

	New Mexico	Hawaii
Remittance of Tax	Tax is remitted monthly by the responsible business to the taxing authority.	Tax is remitted monthly, quarterly or semi-annually by the responsible business to the taxing authority
Activities taxed	Manufacturers and producers, wholesalers, retailers, lessors, service providers, construction contractors.	Wholesaling, manufacturers, producers, retailers, service providers, contractors, lessors.
Is the tax passed on to consumers.	Yes	Yes
Rate structure	5% on all activities	5% on all activities0.15% on insurance commissions .5% on wholesaling, production activities 4% on most consumer activities
Local tax rates	Counties can adopt an additional .50% gross excise tax.	Local jurisdictions can adopt a tax up to 1.875%.
Deductions	Personal property that becomes an ingredient or component part of a manufactured product, property for resale, sub lease of property, services purchased for resale, construction materials purchased by contractors, sub contractor services to construction contractor, purchase of service for export, manufacturers purchase of services performed on tangible personal property, out-of state purchase of personal property for resale, receipts from services performed out-of state, certain sales to farmers and ranchers, sale of tangible property to qualified non-profits, newspaper receipts, bad debts, purchase of personal property and services by filmmakers, sales made to US government, Indian tribes and New Mexico political subdivisions, receipts from sale of prosthetic devices, 50% of the receipts of for profit hospitals, sales of lottery tickets. Non-taxable transaction certificates are required for many of these deductions.	Bad debts, gross income not allowed to be taxed by the Constitution of the US, payments made to a subcontractor by a general contractor if the subcontractor pays the excise tax, certain payments to independent sugar cane producers.

	New Mexico	Hawaii
Exemptions	Gross receipts from items taxed by other statutes (i.e. fuel, oil and gas production, motor vehicle sales, boats, insurance premiums), factors of production, including wages and salaries, receipts of government agencies and non-profit agencies, food stamp receipts, sale of farm products by producers and growers, receipts from feeding or pasturing livestock, interest and dividends receipts, occasional sales, gross receipts generated by items not allowed to be taxed by the US Constitution, sale of tangible personal property to credit unions, receipts from the sale of real property. Non-taxable transaction certificates are required for many of these exemptions.	Gross receipts from items taxed by other statutes (i.e. fuels, cigarettes, liquor, public utilities), food stamp purchases, receipts of exempt non-profits and governmental entities, sales of air pollution facilities, income from subsidized housing, income received by aircraft service and maintenance facilities, casual sales, receipts by a contractor for construction in an enterprise zone, first $2000 of income earned by a disabled person, dividends and distributions, income from the sale of drugs or prosthetic devices, income from the sale of geothermal power , insurance proceeds or damages received for personal injuries or property damage.
Pyramiding	The deductions for ingredients or component parts, purchase of tangible personal property for resale, services purchased for resale, and construction materials, as well as the exception of wages and salaries, interest and rents from gross receipts, are designed to minimize the effects of pyramiding . New Mexico's rate is the same for all businesses to which the tax applies.	Hawaii's tax has been criticized for the pyramiding effect. Most recently by Hawaii's Tax Review Commission.[1] Hawaii's tax on wholesalers and manufacturers is less than on retailers or final service providers.
Use Tax	Yes, applied to goods and services	Yes, applied to goods only.

[1] An example of the pyramiding effect is contained in the commission's report issued December, 1997. A manufacturer produces a good and sells it to a wholesaler for $100. The manufacturer is subject to tax at a rate of 0.5 percent on $100. The wholesaler sells the same good to a retailer for $200. The wholesaler is taxed at a rate of 0.5 percent on the $200. In turn, the retailer sells the good for $300. to the consumer. The retailer is taxed at 4 percent on his gross revenue of $300. In addition, the manufacturer, the wholesaler and the retailer may each include the general excise tax on other goods and services they purchase for their use and which is incorporated into their overhead costs, in their own prices. The committee did decide the breadth and depth of the tax was remarkable and the benefits outweigh the pyramiding effects. The committee did suggest that some of the deductions and exemptions be eliminated or limited to make the tax more equitable and that the legislature limit the effects of pyramiding on lower income individuals through credits on the state income tax or through direct expenditures.

	New Mexico	Hawaii
Tax Exempt Organizations	There are provisions to exempt sales to and sales by tax exempt organizations.	Sales to tax exempt organizations are taxed but the receipts by tax exempt organizations are not.
Revenue Generated	Eighty-seven (87%) of the state's schools expenditures are funded by the gross receipts tax and the state shares 40% of the state's tax collections (including local option taxes) with local governments.	Fifty-two (52%) of the state's income is generated by this tax. The state funds 100% of the school expenditures with this tax.
Other State Taxes	Local property taxes (low when compared to other states), severance taxes, corporate and individual income tax, excise taxes, inheritance tax, real estate transfer tax, insurance premium tax.	Local property taxes (low when compared to other states), corporate and individual income tax, excise taxes, insurance premium tax, inheritance tax, public utility and financial institution tax in lieu of the gross excise tax.

Exhibit B - Hawaii Gross Excise Tax Compared to a Sales Tax:

	Gross Excise Tax	Sales Tax
Imposition	Imposed on the business rather than the customer.	Imposed on consumers who purchase goods or certain services at retail
How Levied	The tax is levied on the gross income of the business activity. It is considered to be an expense which businesses incur in the normal course of doing business.	Sellers are required to charge and collect sales taxes from consumers, usually a percentage of the retail sales price of an item.
Remittance of Tax	Tax is remitted by the business to the state monthly, quarterly or semi-annually.	The tax is remitted by the seller to the state on behalf of the consumer, monthly or quarterly. Certain taxpayers can qualify for direct pay provisions.
Activities taxed	Gross income from almost all types of business activities including tangible personal property at both wholesale and retail, services, contracting, commissions, interest, and lease or rental activities	Retail sale price of tangible personal property and certain designated services,
Is the tax passed on to consumers.	Businesses do pass on the tax to consumers as they do any other business expense, however, businesses are not required to visibly pass on the general excise tax to consumers. The general excise tax law says nothing at all about how the business recovers this expense from the customer. Some businesses in their invoicing or sales receipts have chosen to visibly show the tax.	Since the tax is imposed consumers who purchase goods at retail, it is not passed on to consumers. Sales receipts or invoices are required to visibly itemize the sales tax charged. If the seller fails to collect the tax from the consumer, he still must remit it to the taxing authority.
Rate structure	0.15% on insurance commissions .5% on certain activities such as wholesaling 4% on most consumer activities	Most states have one sales tax rate.
Local tax rates	Hawaii allows counties to levy an additional gross excise tax of .50%.	Local tax rates can be added to the state sales tax rate.

	Gross Excise Tax	Sales Tax
Double taxation	The question arises since both the wholesaler and retailer pays the excise tax, if this is not double taxation. Double taxation occurs when the sale is taxed twice. With the gross excise tax, there are actually two sales transactions. The first one occurs when the wholesaler sells to the retailer and the wholesaler's gross receipts are taxed. The second one occurs when the retailer sells to the consumer and the gross receipts from this transaction are taxed.	In states assessing sales taxes, sales transactions between wholesalers and retailers are not taxed.
Use Tax	Use tax is levied on landed value of tangible personal property imported into Hawaii, and complements the general excise tax by requiring persons importing goods from outside Hawaii to pay the same rate of tax that an in-state seller would have paid in general excise tax had those goods been purchased in Hawaii. A use tax is not applied to imported services though the Hawaii Tax Review Commission has suggested that it be applied to imported services	Most states have a provision for payment of use tax by the purchaser on goods brought into the state for consumer consumption. The rates are usually the same as the sales tax rate.
Are tax exempt organizations exempt from the excise tax.	No, the general excise tax is levied on the business receiving the income not the customer. A business is subject to the general excise tax on transactions with tax exempt organizations because the business is not tax exempt even if their customers are. Tax exempt organizations have the general excise tax passed on to them when they buy goods and services. Tax-exempt organizations are only exempt from paying the general excise tax on certain income they receive.	Yes, since the consumer is responsible for paying the sales tax, states have exempted many organizations from the tax. Many states require that these organizations be issued tax exempt certificates that must be given to or kept on file by the seller.

Nevada Business License

NRS 364A requires all businesses, corporations and partnerships operating in Nevada to have a State Business License issued by the Department of Taxation. A sole proprietorship with one or more employees is also required to have the license. NRS 364A also imposes a tax based on the number of employees working in Nevada or entering Nevada to work or conduct a business activity.

- **WHAT CONSTITUTES A BUSINESS** - Each person, corporation, partnership, proprietorship, business association and any other similar organization that conducts an activity for profit, including an independent contractor or sole proprietor. A trade show or convention held in this state in which a business previously described takes part, or in which a person who conducts such a business attends, for a purpose related to the conduct of the business.

A natural person (sole proprietor) who does not employ any employees, all nonprofit 501(C) organizations and all governmental entities are exempt from the license and tax requirement.

- **OBTAINING A LICENSE** - You may obtain an application (Nevada Business Registration) from the Nevada Department of Taxation office nearest you. When submitted, the application must be accompanied by a $25.00 fee. If the application is from a corporation, the signer's signature is considered a sworn statement of his or her authority to sign on behalf of the corporation. A person who takes part in a trade show or convention held in this state for a purpose related to the conduct of a business is not required to obtain a business license specifically for that event.

All new businesses must show proof of having a State Business License, or sign a certificate of compliance stating they have the State Business License, or are not subject to the requirement before any other license required by a state or local government agency or department is issued.

- **WHO IS SUBJECT TO THE QUARTERLY BUSINESS TAX** - Any business that has employees working in Nevada.

- **HOW AN EMPLOYEE IS DEFINED** - Any natural person who received wages or other remmeration from a business for personal services in this state and a natural person engaged in the operation of a business. This includes persons performing a service in the state for a business located outside this state. This includes, but is not limited to employees the business reports to: (a) Employment Security Department; (b) State Industrial Insurance System (SIIS); or (c) Internal Revenue Service on Form 941, 941M or 943.

The term "employee" does not include: (a) a business, including an independent contractor, that performs services on behalf of another business; (b) a natural person who is retired or otherwise receiving remuneration solely because of past service to a business; (c) a newspaper carrier, or the immediate supervisor of a newspaper carrier who is an independent contractor of the newspaper and receives compensation solely from persons who purchase the newspaper; (d) a natural person who performs all of his duties for the business outside of this state; and (e) an independent contractor who is not an employee of the business with whom he contracts.

- **HOW TO DETERMINE THE NUMBER OF EMPLOYEES** - The average number of employees does not include a sole proprietor or one partner in a partnership. The sole proprietor or one natural person of a partnership shall be considered the employer.

Corporate officers are considered employees if they receive wages, compensation or other benefits for services rendered in this state.

A full-time employee is a person who is EMPLOYED to work at least 36 hours per week regardless of occasional reductions in hours due to sickness, vacation, or other compensated (wages, insurance, benefits, etc.) absence. All other employees are part-time employees and all hours for which such employees are paid must be included in the calculation.

- **RATE OF TAX** - The business tax was enacted effective July 1, 1991. The tax was based on number of employees within a range on a tax table. The tax table ranges and rates are listed on tax returns prior to July 1, 1993.

Effective July 1, 1993, through December 31, 1993, - $25.00 for each employee.

Effective January 1, 1994, - $25.00 for each full-time equivalent employee (calculated to the nearest hundredth or out to 2 decimal places).

- **WHEN TAX IS DUE** - Tax for each calendar quarter is due on the last day of the quarter and must be paid on or before the last day of the month following the quarter.

- **MISCELLANEOUS** -
- For the purpose of calculating the tax, contract or salaried employees will be determined to be full-time unless the employer maintains records showing hours worked to be less than the full-time equivalent.

- Corporate officers or board members not performing a service for the business full time must be included in the calculation of the tax for the period of time they were performing a service in Nevada.

- A general contractor who is required to be licensed under the provisions of NRS 624, must verify at contract inception all subcontractors it hires has a State Business License and have paid their last quarterly payment of the State Business Tax before remitting any payments to its subcontractors.

A subcontractor proves it has a State Business License and has paid the tax by presenting a receipt or other evidence (tax return, canceled check, etc.) showing the last quarterly payment was made. Providing proof of compliance occurs at the time the contractor and subcontractor enter into their initial agreement. If the tax does not apply, a clearance letter from the Department stating a license is not required must be presented.

- Generally speaking, a business is required to keep all records for four years. The same or similar provisions which exist for other Title 32 taxes regarding audits, interest and penalties, confidentiality of information, administrative procedures, etc., are applicable to this tax.

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E-Mail

In action taken May 27, 1999, the Committee voted to recommend further study of the electrical generation tax by the legislature before the tax is considered as a new revenue source for the state.

Public Utility Taxes

Wyoming Public Utility Tax: This tax is currently assessed against the intrastate gross retail operating revenues derived from the provision of telecommunications, gas, electric, water and pipeline service offered for final consumption and not for resale. The purpose of the tax is to fund the operating costs of the Public Service Commission. The rate, which cannot exceed .0030 of the gross Wyoming intrastate retail revenues, is determined by the Director of the Wyoming Department of Revenue and is based upon the budgeted need of the Public Service Commission. The tax is assessed and collected by the Wyoming Department of Revenue.

Other State Taxation of Public Utilities:

Gross Receipts Taxes – Taxes are passed onto customers

State	Tax Description	Rate/Revenue Generated	Disposition of Tax
Alabama	Privilege tax on the intrastate gross receipts of utilities furnishing electricity, domestic water, natural gas, telegraph or telephone services	Varies with utility and receipts (2%-6.7% of gross receipts)/ $14.6 Million	Special Mental Health Trust Fund and the Education Trust Fund
Arizona	Privilege tax on utilities and telecommunications intrastate total income.	State 5%, optional local taxes	
Hawaii	Tax levied against the gross income of public utilities.	State 5.885% is the lowest rate and it increases as the net income of the utility increases	
Illinois	Gross receipts tax on public utilities furnishing electricity, natural gas and telecommunications services.	Telecommunications-7% of gross receipts; Electricity- 5% or $.0032 per killowatt hour per customer, whatever is less; Gas – 5% or 2.4 cents per therm per customer;/ $950 Million tax receipts	State General Fund, Common School Fund
New Jersey	*Public Utility Franchise Tax* on companies providing water and sewer services *Public Utility Gross Receipts Tax* in addition to the Utility Franchise Tax on companies providing water and sewer services. It is in lieu of local taxation. *Public Utility Excise Tax* – Tax on water and sewer companies with $50,000 gross receipts or less and on all utilities except telephone and telegraph	2% of gross receipt $50,000 or less, 5% of receipts exceeding $50,000 7.5% of taxable gross receipts .625% of gross receipts of water and sewer companies less than $50,000. .9375% of all other utilities gross receipts	Local Governments Local Governments Local Governments

State	Tax Description	Rate/Revenue Generated	Disposition of Tax
New Mexico	The state's gross receipts tax applies to the selling of electricity. Deductions are available for selling electricity for resale.	5% plus local option taxes	State and Local governments.
Ohio	Public utility excise tax on the gross receipts of electric, natural gas and telephone utilities	4.75% of gross receipts of all utilities except pipelines which pay 6.75%/$160.1 Million tax receipts	Local Governments-4.2% State General Fund-95.2%
Rhode Island	Tax on gross earnings of public utilities.	Cable Companies – 8% Electric, telegraph and express companies doing business on steamboats – 4% Gas Companies – 3% Telecommunications – 5%	
Texas	Gross receipts tax imposed on each utilities company located in an incorporated city or town having a population more than 1000.	.581% of gross receipts – population of 1,000-2,500. 1.07% of gross receipts – population of 2,500-10,000. 1.997% of gross receipts – population of 10,000 or more	
Utah	A gross receipts tax on electrical corporations whose property tax liability was decreased as a result of property tax reductions by the 1995 legislature.	Gross Receipts in excess of $10 Million –none; receipts in excess of $10 million but less that $500 million, .2363%, in excess of $500 million but less than $1 Billion - .3544%, in excess of $1 billion, .4725%./ $7.1 Million tax receipts	Uniform School Fund
Washington	Public Utility Business and Occupation Tax on public utilities including railroads, express, railroad car, water, electricity, gas, sewer distribution, urban transportation,	Rates will vary according to the service provided.	
West Virginia	*Business and Occupation tax* that applies to the gross income of public utilities excluding electricity and telecommunication companies. *Telecommunications Tax* – A gross receipts tax on local exchange carriers engaged in business of telecommunications within West Virginia.	Water Companies - $4.40 per $100 of receipts Natural Gas Companies - $4.29 per $100 of receipts All Other Public Utilities - $2.86 per $100 of receipts 4% of gross income to services not subject to competition.	

Electrical Generation Tax Based upon Kilowatts – Taxes are passed onto consumers

Alabama	Privilege tax on the manufacture and sale of hydroelectric power within Alabama	2/5 mill on each kilowatt hour of hydroelectric power manufactured and sold.	58% - Special Mental Health fund, 42% Education Trust Fund
Alaska	Electric Cooperative Tax based upon kilowatt hours furnished by qualified electric cooperatives. The tax is in lieu of the corporation income tax.	.00025 per kilowatt hour if cooperative has been in business less than 5 years. .00050 per kilowatt hour if cooperative has been in business over 5 years. $1.5 Million – FY98	If electric cooperative taxes sourced from within municipalities, the municipality receives 100% of the tax. Those sourced outside municipalities are retained by the State.
Idaho	A tax levied per kilowatt hour on electricity generated in the state by water power.	one-half mill ($0.0005) per kilowatt hour/ $3,239,900 tax revenues in 1998	State General Fund
Montana	Electrical energy producers license tax per kilowatt hour produced.	$0.0002 per kilowatt hour produced/ $4.4 Million in tax revenues in 1998	State General Fund
South Carolina	A tax based upon per kilowatt hour of electric power sold by every public utility and cooperative.	one-half mill ($0.0005) per kilowatt hour	
West Virginia	Electric Power Producers pay a tax based upon a formula that computes the average taxable generating capacity (kilowatts) for a four year period. Electric Power Distributors pay a tax based upon kilowatt hour distributed	$20.70 per kilowatt. $0.0019 per kilowatt hour	

In action taken May 27, 1999, the Committee voted not to take individual action on each local tax option considered but to recommend a study of the overall revenue generating authority of local government and its implications before making specific changes to this authority.

Local Tax Options

A. Modifying the purpose of the one-percent capital facilities tax to be used for maintenance of infrastructure.

1) The committee has suggested in its Preliminary Report that the state may have over built its infrastructure. The committee has heard testimony that maintenance of the this infrastructure is a problem.
2) Currently, the one-percent capital facilities tax must be used for specific projects approved by the county's electorate. The project can also include a trust fund for maintenance of the specific project.
3) The suggestion made in this proposal is to allow the tax to be used not only for specific projects but for maintenance of local infrastructure.

B. Local option liquor and cigarette taxes. - This is a suggestion made by WAM

1) Surrounding States

State	Tax	Imposer	Distribution of Revenue
Idaho	Cigarette, tobacco products and liquor taxes	State	General Fund, Alcohol Treatment Funds, College and School Funds, Welfare Funds, Permanent Building Funds and medical funds
	Liquor by the drink tax	Local	Local Government
Utah	Cigarette, tobacco products and liquor taxes	State	Cigarette –General Fund Tobacco Products Tax – General Fund Liquor – General Fund
Colorado	Cigarette, tobacco products and liquor taxes	State	Cigarette – State and Local governments Tobacco Products – State Liquor -State
Nebraska	Cigarette, tobacco products and liquor taxes	State	Cigarette – General Fund, Building funds, outdoor recreation, Department of Health and higher education funds. Tobacco Products – Tobacco Products Administration Cash Fund Liquor Taxes – General Fund
South Dakota	Cigarette, tobacco products and liquor taxes	State	Cigarette- General Fund Tobacco Products –General Fund Liquor Taxes –General Fund and Local Governments
Montana	Cigarette, tobacco products and liquor taxes	State	Cigarette – General Fund, veterans homes and building funds. Tobacco Products – General Fund. Liquor Taxes – General Fund, Department of Health and Human Services, local governments

C. Constitutional amendment to increase mill levies for cities/towns.

1) Depending on the market value of properties in the municipalities, an increase in the mill levies may have less impact in some communities than they would in

other municipalities. Currently, municipalities assess the mill levies optionally. Some municipalities assess their full 8 mills, others assess less or none at all.

2) Assessed values of cities/towns do not reflect the value of minerals.
3) This may be difficult to pass.

D. The Legislature could vote to make the optional general purpose local sales tax permanent and applicable to all local communities.

1) Local officials can make the tax permanent by statute, but hesitate to do so because of the political implications.
2) This suggestion has been made in event the Legislature adopted an additional State sales tax. It is feared that if the state did this, it would impair the passage of the local optional taxes.

E. Additional optional sales taxes for local governments.

1) The state sales tax in some states is not shared with local governments. Instead, these states allow local optional taxes up to certain percentages for local governments.
2) Joe Evans of WCCA believes Wyoming's method of sharing the state sales tax with the communities where it is generated works well. In states that do not have this method, it can be confusing for the taxpayer as he travels throughout the state and also the administrators who must collect and distribute the tax.
3) Surrounding states

State	Tax Source	Distribution
Idaho	State Sales Tax - 5%	Building accounts, environmental accounts, reserve funds, 13.5% to local governments, and 50% to the State General Fund
	County and Municipal Optional Sales Tax Resort County Optional Sales Tax	Local Governments
Utah	State Sales Tax – 4.75%	State General Fund
	Local Optional Sales Taxes- 1% County Optional Sales Tax – ¼% Resort Communities Sales Tax – 1%-1.5% Town Optional Sales Tax – 1%	Local Governments
Colorado	State Sales Tax – 3%	State General Fund
	Local Option Taxes – 1%-4%	Local Government
Nebraska	State Sales Tax – 5%	Sales tax on motor vehicles, trailers and semi-trailers-State Highway Fund, balance to General Fund
	Local Option Sales Tax - .5-1.5%	Local Governments
South Dakota	State Sales Tax – 4%	State General Fund
	Local Option Sales Taxes- .5%-3%	Local Governments
Montana	Local Resort Sales Tax for communities under 5500 population – Rate 3%	Local Community.

E. Increase the assessment percentages for residential, commercial, industrial and agricultural properties.
   1) A one-percent increase for each of these classifications could generate additional revenues of 22.7 million based on 1997 assessment values.
   2) Mineral values would not have an impact
   3) An increase would impact areas where market values continue to increase.

State Lodging Tax

Proposal is to assess the lodging state statewide in addition to the locally approved lodging taxes.

Surrounding States:

State	Tax/Revenue	Distribution
Idaho	Statewide Travel and Convention Tax – 2% tax on lodging facilities Greater Boise Auditorium Tax – 4% tax on lodging facilities	State Treasurer Great Boise Auditorium District
Utah	Rental Vehicle Tax – 3% County Restaurant Tax – up to 1% County Transient Room Tax – up to 4% Municipal Transient Room Tax – up to 1.5% $37.3 Million FY98	Tourist promotion and development operation and maintenance of tourist facilities
Colorado	County Optional Lodging Taxes -.9%-2%	County Tourist Promotions
Nebraska	State Lodging Tax – 1%/ $2.1 Million County Lodging Tax - .5%-2%	State Visitors Promotion Cash Fund County visitor promotion and improvement funds.
South Dakota	Tourism Tax – The tax on visitor attractions, recreational services, recreational equipment and spectator events applies year-around. The tax on visitor intensive businesses applies June-Sept. The tax rate is 1%/ 1.8 Million FY 98	Tourism Promotion Fund and used to promote travel to South Dakota
Montana	Accommodations Tax – 4% Statewide/ $10 Million in FY98	Dept. of Commerce, Preservation Fund, Historical Society, Dept of Fish & Wildlife & Parks and local governments

TAX STRUCTURE OF STATES
WITHOUT THE THREE LEGGED STOOL TAX STRUCTURE

States Without A Sales Tax

	Delaware	Montana	New Hampshire	Oregon
Property Tax	Individual – Residential Land and Improvements Business – Land and Improvements	Individual – Residential land and improvement Business-Land, improvements and personal property Valuable minerals and metals gross proceeds tax-ad valorem tax – 3% of annual gross proceeds. Does not apply to coal, travertine or building stone.	Individual- Land and Improvements Business – Land and Improvements Land use change tax.	Individual – Residential land and improvement Business-Land, improvements and personal property
Individual Income Tax	State –Graduated to 6.9% plus set amount of income over $ 30,000. Local – Varies by municipality	Graduated from 2% to 11% of taxable income.	5% of tax is assessed on taxable interest and dividend income more than $2400.	Graduated from 5% to 9% of taxable income
Other Individual Taxes		Inheritance/estate tax Old fund liability tax –0.2% of employees gross wages.	Inheritance Tax Real Estate Transfer Tax - $.50/$100 of selling price and is paid by both the seller and buyer.	Estate Tax
Corporate Income Tax	8.7% of net income	Corporation License Tax – 6.75% of net income	Business profits tax – 7% of net business income	6.6% of Oregon net income
Excise Taxes	Motor Fuel -$.22/gal. Cigarettes - $.24/20 cigs. Beer - $4.85/barrel Wine - $.97/gal. Liquor-$2.50/gal Lodging – 8% of room charge.	Motor Fuel - $.27/gal Cigarettes - $.18/20 cigs Beer - $4.30/barrel Wine - $1.06/gal. Liquor – 16% of retail selling price of all liquor sold in state Lodging – 4% of room charge Optional Resort Tax – Up to 3% sales tax on goods and services sold by tourist related businesses. Allowed for resort communities under 5500 population.	Motor Fuel - $.18/gal Cigarettes - $.37/20 cigs Beer - $9.30/barrel Wine – State Stores Liquor – State Stores Lodging & Meals – 8% tax on restaurant meals and rooms in lodging establishments.	Motor Fuel - $.24/gal. Cigarettes - $.68/20 cigs Beer - $2.48/barrel Wine - $.67/gal. Liquor – State Stores Lodging – Varies by community.

	Delaware	Montana	New Hampshire	Oregon
Other Business Taxes	Bank franchise tax Corporation franchise tax Gross receipts tax on certain businesses over certain monthly receipts limit.	Cement and gypsum producers license tax Coal gross proceeds tax-5%-assessed on contract price. Coal severance tax- assessed according to BTU and contract price of coal. Contractor's Gross Receipts Tax-1% of public contracts Electrical Energy Producer's Tax-$.0002/kilo produced Liquor License Tax – 10% of the retail selling price of all liquor sold by the state. Metal Mines License Tax – 1.81% of gross proceeds over $250,000 Nursing Facilities Bed Tax - $2.80/per bed/day Old Fund Liability Tax - .5% of gross wages paid to employees. Oil/Natural gas production-rates vary by type of production. Rural Elec/Telephone. Coops-License tax of $10/100 people served, exempt from other excise / income taxes. Telephone License Tax-1.8% of Gross Income	Business enterprise tax - .0025 tax is assessed on taxable enterprise value tax base, which is the sum of all compensation paid or accrued, interest paid or accrued and dividends paid. Tax is a credit against the business profits tax. Real Estate Transfer Tax - $.50/100 of the selling price and is paid by both the seller and buyer.	Railroads and Investor Owned utilities - .25% of operating revenues of utilities, .35% on gross operating revenues of railroads Amusement Device tax – Tax paid on gaming machines Timber Severance Tax-Paid by timber owners on harvested timber's value. Forest Products Harvest Tax-Paid on timber cut from any land in Oregon

States without an Individual Income Tax

	Alaska	Florida
Property Tax	At the option of the borough or the municipality. Mill levies are assessed against real property Petroleum Property Tax – 20 Mills on the full and true value of taxable property	Individual – Residential land and improvement Business-Land, improvements and personal property Intangible Personal Property Tax-A/R, stock, trusts, notes, bonds, loans to and from shareholders, limited partnership interests.
Other Individual Taxes	Estate Taxes	Estate Taxes
Sales and Use Taxes	No statewide sales taxes. Sales taxes are at the option of the individual boroughs or municipalities	State (6%) plus local option sales taxes
Corporate Income Tax	1%-9.4% of Corporate net income Petroleum Corporation Income Tax	5.5% of net income
Other Business Taxes	Electric and telephone coop tax – Tax based on revenue Fisheries Business Tax-1%-5% of the value of fish paid to fishermen. Fishery Resource Landing Tax – 3.3% of average price/pound of fish landed Salmon Enhancement and Marketing Taxes	Severance Taxes Insurance premium taxes Gross Receipts Tax
Excise Taxes	Motor Fuel -\$.08/gal. Cigarettes - \$1.00/20 cigs. Beer - \$10.85/barrel Wine - \$.85/gal. Liquor-\$5.60/gal Lodging –At the option of the municipality	Motor Fuel -\$.128/gal. Cigarettes - \$.339/20 cigs. Beer - \$14.88/barrel Wine - \$2.25/gal. Liquor-\$6.50/gal Lodging –State lodging and local option taxes.

States without an Individual or Corporate Income Tax

	Nevada	South Dakota	Texas	Washington	Wyoming
Property Taxes	Individual – Residential land and improvement Business-Land, improvements and personal property Oil and gas conservation tax – 50 mills	Individual – Residential land and improvement Business-Land and improvements Conservation tax on energy minerals – 2.4 mills of taxable value	Individual – Residential land and improvement Business-Land, improvements and personal property	Individual – Residential land and improvement Business-Land, improvements and personal property	Individual – Residential land and improvement Business-Land, improvements and personal property Ad valorem tax on the gross production value of minerals
Other Individual Taxes	Estate Tax	Estate and inheritance taxes	Estate Tax	Estate Tax Real Estate Transfer Tax – 1.28% of selling price	Estate Tax
Sales and Use Taxes	State (6.5%) plus local option taxes	State (4%) plus local option sales taxes Vehicles & snowmobiles – 3%	State (6.25%) plus local option sales taxes that bring the tax to a maximum of 8.25% Motor vehicle & boat sales are taxed at 6.25% Manufactured homes are taxed at 5% on 65% of the purchase price of the retailer.	State (6.5%) plus local option taxes. Refuse collection tax – 3.6% on the cost of service. Rental Car Tax – 5.9% on the cost of rental.	State (4%) plus local option taxes

	Nevada	South Dakota	Texas	Washington	Wyoming
Other Business Taxes	Insurance Premium Tax – 3.5% of net premiums State Business Tax - $25/ employee/quarter. Levied on all businesses for the privilege of doing business in Nevada. Gaming Taxes Net proceeds minerals tax – 2%-5% of net proceeds or minerals earned from mining.	Bingo/Pull Tab Tax Contractors' excise tax-State(2%) plus municipal(.5%) on gross receipts of contractors for realty improvement contracts. Energy minerals severance tax – 4% of taxable value. Precious metals tax – $4 per ounce of gold production plus 10% of net income Banks and Financial Institutions-6% decreasing to 1% as net earnings increase. Tourism Tax –1% tax during June, July, Aug & Sept. on the gross receipts of tourist intensive businesses.	The Franchise Tax – Tax paid on the greater of the net taxable capital or net taxable earned surplus. Rate for taxable capital is 0.25%/yr. The rate for earned surplus is 4.5%/yr. Gas Production Tax – 7.5% of the market value of gas produced Oil Production Tax – 4.6% of the market value of oil or 4.6Cents for each 42 gallons of oil produced which ever results in the great amount of tax. Sulphur Production Tax - $1.03 per long ton of sulphur produced Cement Production - $.0275 for each 100 lbs of cement produced Oil Well Service Tax – 2.42% of gross receipts after the deduction for materials. Gross Receipts Tax – Tax on gross receipts of gas/electric/ water utility cos. operating in towns with a population of 1000 or more. In addition a tax of 1/6 of 1 percent of gross receipts is assessed all public utility cos. Insurance Taxes – 12 different taxes incl. insurance premium and maintenance taxes. Attorney Tax – Each active attorney pays a $200. tax/ year.	Business and occupation tax-Rates depend on type of business and is assessed against the gross income of businesses . Public utility tax – Tax assessed against the gross operating revenue of public & privately owned utilities. Insurance premium tax – Tax assessed on gross premiums. Timber excise tax – Assessed on the stumpage value of timber. PUD excise tax – Tax assessed on the privilege of producing energy by public utilities Leasehold excise tax – Tax assessed on the rental value of leased publicly owned property. Entertainment tax – Tax on pari mutual machines and ticket sales for boxing / wrestling matches. Food fish & shellfish tax-Tax paid by the first commerical processor of fish. Carbonated Beverage Tax - $1.00/ gallon of syrup. Municipal Business Taxes – Percentage of gross revenues paid to city clerks for the privilege of doing business within a municipality.	Mineral severance tax -2%-7.5% on the gross production value. Insurance premium tax Corporation franchise tax.

	Nevada	South Dakota	Texas	Washington	Wyoming
Excise Taxes	Motor Fuel -$.23/gal. Cigarettes - $.35/20 cigs. Beer - $2.79/barrel Wine - $.40/gal.base Liquor-$2.05/gal over 21% Lodging Tax –State (1%) tax plus local option lodging taxes.	Motor Fuel -$.21/gal. Cigarettes - $.33/20 cigs. Beer - $8.37/barrel Wine - $.93/gal.base Liquor-$2.72/gal	Motor Fuel -$.20/gal. Cigarettes - $.41/20 cigs. Beer - $5.89/barrel Wine - $.20/gal.base Liquor-$2.40/gal Mixed beverage gross receipts tax – 14% on the gross receipts from the sale or service of alcoholic beverages. Lodging Tax –State (6%) tax plus local option lodging taxes up to 9%.	Motor Fuel -$.23/gal. Cigarettes - $.825/20 cigs. Beer - $8.08/barrel Wine - $.87/gal.base Liquor-$9.24/gal Mixed beverage gross receipts tax – 20.5% on the gross receipts from the sale or service of alcoholic beverages. Lodging Tax –2% of sales tax on room plus 2%-3% of room cost.	Motor Fuel -$.14/gal. Cigarettes - $.12/20 cigs. Beer - $.62/barrel Wine - $.28/gal.base Liquor-$.95/gal Lodging Tax –1% -4% of room rate at local option.

WASHINGTON BUSINESS AND OCCUPATION TAX

What is a Business and Occupation tax:

The Washington State Business and Occupation (B&O) tax is similar to a gross receipts tax. In Washington, though, it is a tax in addition to the state's sales tax. Washington does not have a Corporate or Individual Income Tax. The tax is a tax on the gross receipts (gross income, gross sales or value of products) of all businesses operating in Washington as a measure of the privilege of engaging in business. The state government has a B&O tax as well as local counties and cities. The local B&O taxes are assessed and collected locally.

Tax Application:

Almost all businesses located or doing business in the state of Washington are subject to the state B&O tax. This includes corporations, partnerships, sole proprietorships and nonprofit corporations. A sale does not have to occur for a business to owe the B&O tax. Examples of activities without a sale which create a B&O tax liability include the internal distribution of products from a business' central warehouse to two or more of its retail outlets, and extracting or manufacturing goods for a businesses own use. The tax is calculated on gross income of the business from activities in the state. There is no deduction from the tax base for labor, materials, taxes or other costs of doing business. A business may qualify for exemptions, deductions or credits.

Tax Rates:

Thirteen different tax rates for various classifications of business activities.

Manufacturing, wholesaling, and other activities	.484%	Retailing	.471%
Stevedoring & freight brokers	.363%	Manufacturing fruit and vegetables	.330%
Processing of meat (wholesale), soybeans, canola, wheat into flour & raw seafood products	.138%	Travel agent commissions, manufacturing nuclear fuel, processing dry peas, international investment management	.275%
Wholesaling of wheat, corn barley, canola, dry peas and beans, oats, lentils and triticale	.011%	Insurance Agent/broker commissions	.550%
Public and nonprofit hospitals	1.5%	Disposal of low-level radioactive waste	3.30%

Selected business services: clerical, computer, information, legal, accounting, engineering, business management, protective, public relations and advertising and surveying and real estate appraisal	1.5%	Financial Services: banking, securities and investment management, investment advising.	1.5%
Service and other activities: i.e. physicians, dentists, teachers, beauticians	1.5%		

Tax Administration:

Tax is paid to the Washington Department of Revenue monthly, quarterly or annually. A business must be registered with the Department of Revenue if the gross income is $12,000 a year or more or if they collect or pay other taxes to the department. If a business's annual revenues are $24,000 or less, a tax return does not have to filed.

Exemptions:

Exempt activities are not subject to the B&O tax and do not need to be reported to the Department of Revenue.

Farming – raising animals or fish for sale, raising Christmas trees, sponsoring agricultural fairs, producing eggs and poultry, processing hops into extract, pellets or powder so to out-of-state buyers, small timber harvesters whose income is less than $100,000.

Nonprofit and social service organizations – occasional sales, Red Cross functions, rehabilitation services to the handicapped, services of fraternal benefit societies, certain medical facilities, government grants and tuition charges, student loans, auctions by non-profits, blood, bone and tissue banks, child care resource and referral income, adult family homes, ride sharing transportation services for commuters and elderly.

Government – County, city, school and fire district income, state and federal grants received by political subdivisions, state housing finance commission.

Financial – International banking facilities, state and federally chartered credit unions.

Miscellaneous – Out of state firms which sell consumer products in Washington through representatives and not retail outlets.

Deductions:

Amounts that are deductions must first be included in gross income and then identified and deducted from gross income.

Farming: preparing and packing fresh horticultural products when done for commercial farmers, packing materials for fresh horticultural products, interest on loans to farmers by production credit associations.

Nonprofit and social service organizations: Membership fees and charges for recreational activities by youth organizations, business income of artistic and cultural organizations, federal, state, city or county payments to health and social welfare organizations.

Government: charges of services among political subdivisions, payments by municipal sewerage utilities to other public agencies.

Financial institutions: Interest derived from first mortgage loans on residential property, interest from government obligations issued by State of Washington and its political subdivisions.

Miscellaneous: Fees of private day care centers, investment income received by non-financial businesses and dividends received by a parent corporation from subsidiaries, activities prevented from taxation by the US constitution, bad debts sustained by sellers, maintenance fees paid by residents of cooperative housing associations, reimbursement of expenditures received by funeral homes for services rendered by others, amounts received by sponsors of trade shows, seminars and conventions if events are not open to the public.

Credits:

Credits are subtracted from the B&O tax due on the tax return.

- Business and Occupation tax credit for small businesses
- Bad debt tax credit
- Distressed area B&O tax credit
- Multiple activities tax credit
- Credit for overpayment of taxes
- High technology business and occupation tax credit

Major Issues:

The B&O tax produces a much larger proportion of total state revenues than does the corporate income tax in most other states. The tax burden initially imposed upon business is relatively high compared with other states especially when the sales tax is considered. Most businesses are subject to the B&O tax, but those who are not required to collect sales tax have less of a burden under the Washington tax system.

The advantages of the tax include:

a) It is easy to understand, simple to calculate for taxpayers and auditing is relatively simple. There is no need for businesses to apportion income among states as is the case for multi-state corporations paying corporate income taxes.
b) The tax is deductible for federal income tax purposes.
c) There is no discrimination for payment of tax due to the structure of the firm; corporate and non-corporate structures are treated the same.
d) Firms can project sales better than profits and therefore may be able to include the tax in the prices they charge, if market conditions permit.
e) It assures that profitable businesses and those organized as non-profit, as well as unprofitable enterprises (including those that intentionally operate at low profit margins by paying abnormally high salaries to owners) pay some tax for the government services they receive.
f) Economically it encourages firms to operate with maximum efficiency.
g) It is a productive and stable revenue source for government collections; collections do not fluctuate during economic downturns to the same extent as other tax sources.

The disadvantages of the tax include:

a) It imposes a heavier burden on new and small businesses who have not met the optimum level of operating efficiency or have fully developed their markets, and as a result are unprofitable. The tax does not encourage economic development.
b) There is continual pressure on the legislature to grant new preferential tax rates for industries in economic difficulty or are in a poor position to pass along the tax in their pricing structure.
c) One of the state's major industries, agriculture, is not subject to the tax
d) The tax pyramids for sales to other firms at each level in the chain of production and favors vertically integrated firms taxed only upon the income derived from the final sale of the product.

e) The tax favors low-volume high profit types of firms, whereas it can be much more difficult for low-profit activities that depend upon greater turnover of products.

Tax Income Generated:

All tax revenues of the business and occupation tax are deposited to the state general fund. The tax in 1995 generated 16.6% of the income for the state general fund.

Other State Taxes:

Sales and use taxes (state and local), excise taxes (motor fuel, cigarette, tobacco products, liquor, brokered natural gas, rental car, refuse collection), public utility tax, insurance premium tax, state and local property taxes, taxes in lieu of property tax (vehicle excise tax, PUD excise tax, timber excise tax, leasehold excise tax), inheritance taxes, real estate transfer tax, pari-mutual tax, boxing and wrestling tax, food fish and shellfish tax, hazardous substance tax, carbonated beverage syrup tax, petroleum products tax, oil spill tax, lodging taxes.

TEXAS CORPORATE FRANCHISE TAX

Application of the Tax:

The tax is imposed on each corporation that is chartered in Texas or has a Certificate of Authority to do business in Texas. It is also imposed on banks, limited liability companies, S corporations, state limited banking associations, savings and loan associations, professional limited liability companies and professional corporations. It is not imposed on proprietorships, partnerships, limited liability partnerships, and professional associations. In concept the franchise tax is a license or "privilege" tax. Corporations pay it for the right to do business in the state and in return the state grants the corporation certain rights.

Any corporation that is chartered in Texas is subject to the tax, as is a foreign corporation with nexus in Texas. To have nexus the corporation must have one of the following:

- a physical presence in Texas either by owning or leasing property or by having employees
- a general partner in a Texas limited partnership
- independent contractors in Texas to promote sales in the State
- theatrical performances in Texas
- independently owned franchised businesses.

Tax Administration:

The tax is due annually to the Comptroller of Public Accounts by May 15 of each. In general, the tax report should be based on business done during the corporation's accounting year that ended in the prior calendar year.

Tax Base:

Corporations pay the greater of the tax on net taxable capital or net taxable earned surplus.

<u>Tax based upon capital</u>

Taxable capital is a corporation's net worth or shareholder's equity. The computation of the tax is very complex.

Tax based upon earned surplus

As a tax on profits, it is similar to the federal definition of net taxable income. It is calculated as followed:

	Federal Taxable income
Plus:	Amount claimed on the federal return for the net operating loss deduction (Texas disallows this deduction)
Minus:	Certain income from foreign sources included on the federal return
Plus:	Officer/director compensation (corporations with less than 35 shareholders and s-Corporation do not add this)
Equals	Total Earned Surplus

Once the tax base is determined, it is apportioned to Texas. Federal law requires that a state's tax on net income of a multi-state corporation reflect the activity of the corporation in that state. Capital and earned surplus are apportioned to Texas by using the ratio of the business's gross receipts from business performed in Texas to the total gross receipts of the company.

Tax Rate:

The tax that is due is the greater of .25% percent of the corporation's Texas apportioned capital base or 4.5% percent of the apportioned earned surplus. If the tax is less than $100.00, no tax is due.

Texas's corporate taxes are among the nation's lowest—however this is offset by state's high local property taxes.

Who pays the Franchise Tax:

An overwhelming bulk of the franchise tax is paid by the state's largest businesses. Less than 2% of all corporations had over $100 million in total business receipts but they accounted for over half of Texas Franchise taxes. Three-fourths of Texas corporations doing less than $1 million in business account for 8% of the tax. In 1997, there were 360,000 corporations subject to the tax but only 100,000 paid the tax.

Tax Income Generated:

The tax is Texas's third largest source of tax revenue behind the sales and motor fuel taxes. Corporations paid $1.8 billion in franchise taxes in 1997, 9% of all state taxes. The earned surplus option was instituted in 1991 and since that time there has been continued increase in revenues from the tax. The economy has been healthy since 1991 which can also attribute to the increase in franchise tax collections. It is uncertain what would happen to tax revenue in event of a recession. Most corporations pay the tax based upon the earned surplus calculation. Since profits are volatile, tax revenues could decrease in a recession. The decline could be mitigated somewhat by the capital tax calculation which operates like an alternative minimum tax.

Major Issues:

Four criteria has been used to evaluate the tax:

<u>Adequacy</u> Since 1992 the tax has generated adequate revenue in a stable and predictable manner. There has been an annual rate of growth of 10.5%. Tax collection increases are attributed to the increase in Corporate profits. Corporate profits can be volatile and the tax has not had a sufficient tract record to adequately evaluate the long term adequacy of the tax.

<u>Equity</u> In 1987, the Select Committee on Tax Equity said the tax was inequitable across industries. At that time, the franchise tax was based solely on capital and was a burden for capital intensive corporations. The restructuring of the tax in 1991 to include the earned surplus method of computation has helped to defray this criticism though capital intensive industries still have a greater burden than service industries.

The select committee also stated the tax does not apply to the general business community but is limited to corporations and limited liability companies. Today, there are other forms of business organizations that enjoy the benefits granted corporations in the past which was the rationalization for the franchise tax, yet they are not included as businesses taxed. The decision to organize as a corporation triggers the franchise tax liability which unincorporated firms do not bear. Businesses may opt for a form of organization not taxed in order to avoid the franchise tax in the future. This could affect future tax revenues.

<u>Economic Efficiency</u> The Texas franchise tax is favorably competitive with tax systems in other states. Both the capital and the earned surplus tax bases contain few of the tax incentives and deductions seen in some other states—keeping the tax base fairly broad and allowing overall rates to remain very competitive with other states.

Ease of Administration   The earned surplus option is easy to administer for both the payer and the administrator since it draws from the federal taxable income. The capital tax computation is complex and generally only understood by tax professionals. It also imposes high administration and audit costs.

Other State Taxes:

Sales and use tax, local property taxes, amusement machine tax, excise taxes (cigarettes and tobacco, liquor), motor fuel taxes, mineral taxes, mix beverage gross receipts tax, motor vehicle and boat sales tax, oil well servicing taxes, lodging taxes, utility company gross receipts tax, inheritance tax, insurance premium tax, telecommunications infrastructure fund tax.

MICHIGAN SINGLE BUSINESS TAX

What is the Single Business Tax (SBT).

It is the only general business tax levied by the State of Michigan. It was enacted in 1976 to replace seven business taxes, including the corporate income tax. The SBT replaced net income-based taxation with value added taxation. The SBT base consists of essentially three components: labor, capital and profit. Labor is measured by the compensation and benefits an employer pays to its employees; capital used is measured by depreciation, interest, dividends and royalties paid by the taxpayer; and profit is measured by the taxpayer's federal taxable income as adjusted for SBT purposes.

The Application of the SBT Tax

All persons engaged in a "business activity" in Michigan are subject to the SBT. Business activities include: the sale of real or personal property in return for tangible or intangible consideration, property rental, including both real property and personal property, performance of a service for a fee, except services rendered as an employee or services rendered as the director of a corporation.

Only firms actually engaged in business activity in Michigan are subject to the SBT. A foreign subsidiary or parent corporation with no Michigan business activity is not subject to the SBT

Any "person" engaged in a business activity in Michigan whose adjusted gross receipts are $250,000 or more in a tax year is required to file a return.

A "person" is an individual, firm, bank, financial institution, partnership, limited partnership, co-partnership, joint venture, association, corporation, limited liability company, receiver, estate, trust or any other combination acting as a unit.

Gross receipts include all receipts derived from a business activity including rental and lease receipts. Adjusted gross receipts means apportioned gross receipts from a business activity plus capital acquisition deduction recapture.

Tax Base and Tax Rate

Exhibit A shows how the SBT tax is calculated as a VAT. The SBT liability starts with the calculation of the total tax base. The primary components of the tax base are compensation, business incomes as defined for federal tax purposes, and additions or subtractions to federal business income.

- Compensation includes salaries, wages, employee insurance plans, retirement benefits and pension and profit sharing plans. Compensation does not include FICA, unemployment insurance or worker's compensation.

- Additions to federal business income deprecation, taxes based on income, net operating loss carryover or carryback and any dividend, interest and certain royalty expense taken on the federal return.

- Subtractions from federal business income dividend, interest and certain royalty income reported on the federal return

- Deductions are allowed for the cost of capital acquired during the tax year, while an addition is required for proceeds from the sale of such items.

- There are numerous other exemptions, reductions and credits that may be allowed. These modify the value added nature of the SBT and reduce the tax liabilities for firms that qualify to use them.

Firms doing business in Michigan and in other states apportion their tax base to Michigan using a formula based on their percentage of property, payroll and sales in Michigan. In 1999, the appor tionment will be 90% sales, 5% property and 5% payroll. Financial organizations and transportation companies use a single factor formula based on gross business and revenue miles, respectively.

Once the total tax base is determined it is multiplied by the tax rate, then the eligible tax credits are subtracted from the tax due. The SBT rate is 2.30 percent of the tax base after deductions.

Tax Exemptions:

- Most persons who are exempt from federal income tax under the Internal Revenue Code

- Nonprofit cooperative housing corporations.

- Farmers producing agricultural goods.

- Partners of partnerships and shareholders of Sub S corporations. Partnerships and Sub S corporations are subject to the SBT.

Tax Credits:

There are credits for small businesses, the Unincorporated/S corporation Credit, the Community Foundation Credit, the Homeless Credit, the Public Contribution Credit, the Public Utility Property Tax Credit, the Michigan Economic Growth Authority Credit, the Brownfield Redevelopment Credit, the Apprenticeship Red and the Renaissance Zone Credit.

Tax Administration:

The return is due on the last day of the 4th month after the firm's tax year ends. It must be filed by the same tax period covered by the federal income tax return. If the estimated tax liability for the year is over $600.00, quarterly estimated filings are made.

Tax Issues:

Comments of Mark Haas, Director of Finance and Fiscal Policy, Michigan Department of Treasury, at the Minnesota Taxpayer's Association meeting, June 10, 1998.

With the adoption of the SBT in 1976, Michigan's theory of business taxation shifted from the "ability to pay" to "benefits received". Before the change if you had profits, you paid, if you didn't you did not pay. After the change, if your business operated, you paid. This meant that even in recessions, business paid taxes to help fund the services that still had to be maintained.

In theory, there are three types of Value Added Taxes (VAT):

- The Gross Products VAT – Allows no deduction for capital investment and provides no incentive to invest in capital.

- The Income VAT – Allows depreciation deduction so that the incentive is to spread investment over the life of capital assets.

- The Consumption VAT – Provides immediate write off of capital purchases, usually with a carry forward of unused write-off amounts. This is the version used in Michigan and provides the greatest incentive for capital investment.

Pure theory has there are two ways to calculate a "value added" tax base.

- Subtraction Method – Cost of materials purchased is subtracted from the sales revenue of products or services sold.
- Addition Method – You consider what are the pieces of the final price. Pieces include cost of materials, cost of labor, cost of equipment, interest on loan proceeds used in the production process and some amount of profit. You add all the pieces together and subtract the cost of materials.

Once you get to the legislative process, pure theory does not remain so very long. In Michigan that was the case.

- To cut administration expenses, Michigan starts its value-added calculation with the federal adjusted gross income, the profit piece, adds to this figure compensation including benefits but not FICA, unemployment or workmen compensation expenses. Also added are the costs of capital, depreciation and dividends and interest paid.
- The SBT in Michigan in 1976 replaced 7 business taxes. Over the years, different businesses, legislators and governors have come up with different ideas as to what the SBT should be. Different firms were affected differently by the change from a profits tax to the SBT. The firms asked for and received special treatment.
- Currently, there a four ways to figure a firms tax liability under the SBT. 1) The straight percentage method, 2) the gross receipts method which taxes total sales, 3) the alternative tax method which works like an income tax, and the 4) excess compensation method which is a modified VAT that gives a break to labor intensive firms.

What does the Michigan SBT generate:

1994-1995 Michigan Tax Base

Federal Taxable Income	15,000,000,000
Compensation	98,000,000,000
Other additions and subtractions.	30,000,000,000
"Pure VAT Base"	$143,000,000,000
Capital Acquisition Deduction (CAD)	22,000,000,000
Business Loss Deduction	4,000,000,000
Statutory Deduction for small businesses.	2,000,000,000
Adjusted Tax Base	$115,000,000,000
Excess Compensation Deduction	11,000,000,000
Gross receipts alternative calculation deductions	7,000,000,000
Reduced Tax Base	97,000,000,000
Tax Rate:	2.30%
Taxes Generated before Credits	$2,231,000,000

The reduced tax base is two – thirds of the pure tax base. 175,000 firms filed SBT returns and 105,000 firms benefited from the CAD deduction, 51,000 firms from the excess compensation deduction, 37,000 from the small business deduction, 23,000 from the gross receipts tax alternative and 78,000 firms from other deductions.

Who pays the SBT?

A relatively few large firms pay most of the SBT.

- 84 firms with the largest SBT tax bases (over $100 million) comprised 0.1% of all firms yet paid 32% of all revenue collections.
- 1545 (1% of all firms) companies with tax bases over $10 million paid 57% of the taxes collected.
- The top 2600 firms (1.6% of all firms) pay almost 65% of the total tax.

Distribution of the SBT among industrial sectors

- Manufacturing - 45.6%
- Finance and real estate -- 7.7%
- Transportation Equipment (including auto companies) -- 18%
- Services -- 15.7%
- Retail -- 12.6%

Strengths of the SBT:

- The SBT tax provides a more stable source of government revenue. Figure 6, shows that if Michigan would have had a corporate income tax at a rate (11%) that would generated the same revenues in 1996 as the SBT, revenue generated by a corporate income tax would have been markedly different than the actual revenues generated by the SBT during the previous eight years. During periods of recession, the SBT tax shows more stability than a corporate income tax. The question arises whether a state wants the kind of stability offered by the SBT or a tax that provides less stability but is based upon a taxpayer's ability to pay. This can be answered by such questions as how does a state legislature react to revenue windfalls.

- The SBT tax is considered to be more neutral across types of firms. The two biggest special provisions of the SBT—the CAD and the excess compensation reduction are obviously non-neutral, taken alone, but together their effects tend to cancel out. There has also been no tax rate increases for the SBT since its inception. The SBT is also neutral with respect to the firm's choice of organization. All organizational forms are taxed.

Weaknesses of the SBT:

The SBT is very unpopular with non-profit or low-profit firms. Businesses get very angry when they are losing money. Even when they are losing money they consume business services.

The SBT apportionment is quite arbitrary. The question arises as to when you determine value is added. There have been many court challenges on this and other SBT issues. Currently, there are half a dozen major lawsuits outstanding. It is difficult to anticipate future revenues, when lawsuit decisions could amend tax calculation bases.

Response of business to the switch from the profits tax to the SBT:

There has been more capital investment in manufacturing than would otherwise have occurred.

Business makes a constant effort to reduce the tax base. Since 1991 there have been several increase in the filing thresholds (1991-$40,000, 1998-$250,000), apportionment changes, exceptions for unemployment insurance and workmen compensation payments, other base changes and special provisions.

There has been a dramatic change in the way firms file their SBT. In 1988-89, half the firms used the straight percentage method (the basic value added method) and 4% used the alternative rate method (a type of income tax). It is estimated that by 1998, one-third will use the VAT method and 20% will use the alternative method.

Summarization:

If a state follows Michigan's experience and enacts a SBT, the state will have:

- revenue stability
- many special provisions
- an original tax base that will erode over time
- constant litigation on interstate commerce issues
- a lot of work for CPA's hired both for the administrator and the taxpayer.

Other State Taxes:

Individual Income tax, Property tax, Sales/use tax, Intangible and Estate Tax, Severance tax on oil and gas production, Excise taxes (tobacco, liquor and motor fuel)