

MMA Testimony House Tax Policy Committee October 28, 2009

Good morning Madam Chair and committee members,

Thank you for the opportunity to voice our views on tax rates in the Michigan Business Tax. These issues are important to MMA members and to the Michigan economy. In my comments this morning, I would like to outline how important manufacturing is to the Michigan economy. Then I would like to talk about the MBT credits, and make the case for the need for a rational economic policy in Michigan.

As I have said in this committee before, manufacturing is the largest sector in the Michigan economy by wide margin. Manufacturing makes up 20 % of the gross state product. The next largest sectors are tied at 12% and they are real estate (rental and leasing) and government. In comparison, Retail is only 7% of the total Gross State Product, Health care is only 8%, Professional Services is only 8%, and Construction is only 3%.

Manufacturing employs about 500,000 people in Michigan.

Despite the economic downturn, manufacturers have invested billions in capital investment in Michigan over the last decade. General Motors has invested \$10 billion in the last five years, Ford has invested \$13 billion since 2000. Hemlock Semi Conductor recently invested a billion in Hemlock, Michigan. Several advanced battery companies are investing here, A123 systems is investing \$600 million, Johnson Controls-Saft is investing \$200 million, to name just a few examples.

The manufacturing sector is distinctly different from other sectors of the economy in some very important ways:

It generally requires significant capital investment, both real and personal property.

Relatively high wages to other sectors and good benefits.

Competes on the basis of cost in the global economy – not true of other sectors.

High economic multiplier effect – all manufacturing sectors.

- Example - Center for Automotive Research reports the auto sector generates on average 7.6 jobs for every job in an OEM.
- The challenges in Michigan's economy demonstrates an economic divisor effect in Michigan – the effects down the supply chain. When manufacturing investments are more attractive elsewhere, the effect is seen in arithmetic terms.

- Michigan's future is inextricably tied to manufacturing.

MBT Credits

The credits in the MBT, identified in the committee's agenda are there for generally two purposes. First, they are intended overcome the disproportionality of the personal property tax in Michigan and by the gross receipts tax imposed on the manufacturing sector.

While most states have eliminated this tax, Michigan continues to impose this disincentive to investment in production equipment in Michigan. Michigan's gross receipts tax is generally considered a unique nationally. Secondly, the credits were designed into the MBT to attract the things we want the most in Michigan - jobs, capital investment, and research and development. These positive economic activities are particularly characteristic of the manufacturing sector. So, reductions in these credits are direct tax increases on manufacturers with little to no tax increases on other business sectors.

It is especially important to note that credit reductions only impact Michigan's home team and do not export any of the tax increases to out of state firms. Let me say that again, credit reductions for personal property tax, compensation, investment tax credits, and research and development will result in direct tax increases on the home team, those that have invested here, hired people here and developing products here, and exempts out of state companies with MBT liability.

The focus on credits may be looking too narrowly. Ultimately, companies look at the bottom line tax obligations. We should be looking at how Michigan tax policy stacks up against other competitor states in taxing manufacturers. I think you will find that Michigan does not stack up well durable goods manufacturers.

Michigan's History Troubling Pattern of Overtaxing Its Industrial Base.

Michigan has a troubling tendency to increase taxes on manufacturers when the economy turns down. Take for example, the MBT surcharge. When the MBT surcharge was established to replace the ill-conceived service tax in 2007, manufacturers took a disproportionate hit. While everyone is aware the surcharge imposed a 21.99% tax on all MBT payers amounting to about \$700 million, it is not widely understood that an additional hundred million dollars was imposed in the form of reductions in the credits in the MBT. Specifically, reductions in the compensation, investment tax credit and research and development credits. Again, these tax increases were born largely by manufacturers. Then, when the surcharge was imposed on all MBT payers, including manufacturers, none of the credits were eligible to be used against the surcharge, creating an additional burden specifically on manufacturers.

The tendency to tax manufacturers more in a down turn is well recognized by manufacturers inside and outside of Michigan, and it is not a good for economic development in Michigan.

Michigan needs a rational economic policy.

Michigan needs a rational economic policy. Currently, Michigan's tax policy is completely opposite from most states. Most states tend to tax businesses and particularly manufacturers relatively less and the consumption side off the economy relatively more.

- Michigan needs to eliminate the disproportion burden placed the industrial sector. Michigan has a very high effective tax rate on durable goods manufacturers compared to the national average. Yet, business taxes for all businesses are on average only slightly above the national average. Michigan's personal income taxes and sales taxes are relatively low compared to the national average.

- Michigan needs to eliminate the personal property tax. If we didn't have the personal property tax we wouldn't need the personal property tax credits. Michigan continues to impose the personal property tax, while most states have eliminated it. The PPT is a direct tax on production equipment. It should be no surprised that Michigan's unemployment rate is 15.2% compared to the Midwest average of only 10%.

- Michigan needs to eliminate the MBT surcharge and restore the credits to the pre-surcharge levels.

- Michigan needs to understand that other states and nations want Michigan's industrial infrastructure and they are working aggressively everyday to lure it away. Ohio eliminated the personal property tax on industrial equipment. Other states are offering Michigan companies upfront money, job training and land. Other states have recruiting offices here in Michigan.

- Michigan needs to reduce taxes on jobs, capital investment and R&D. These are the drivers of economic activity. We should not be increasing taxes on these things. Even discussions about tax increases tend to scare off potential investors, because it highlights Michigan's tendency to tax manufacturers more in tough times.

A rational economic policy also includes reducing the size of state government. Manufacturers cannot compete on the basis of cost in the global economy, if the cost of state government cannot reduce its costs on manufacturers.

A rational economic policy will allow Michigan to attract job creating industrial investment, and attract R&D projects that create new products here in Michigan. Michigan's economy will rebound when more people are working, paying income tax, spending money in other parts of the economy, and paying sales tax. Michigan can become great again, but we need to act quickly.