Legislative Analysis

BONUS DEPRECIATION

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House Bill 4324 as reported from committee
Sponsor: Rep. Luke Meerman
Committee: Tax Policy
Complete to 4-9-21

SUMMARY:

House Bill 4324 would amend the definition for federal taxable income in the Income Tax Act to allow the bonus depreciation allowance present in federal tax law to be applied when calculating a taxpayer's state corporate income tax.

2008 PA 434 added the following to the definition of ***federal taxable income***, which previously mirrored the definition in the federal Internal Revenue Code: *except that federal taxable income shall be calculated as if section 168(k) and section 199 of the Internal Revenue Code were not in effect.*

The bill would remove that italicized language, to return the definition to its pre-2008 form.

Section 168(k) of the Internal Revenue Code governs "bonus" depreciation—or the provision that allows a taxpayer to claim more of the purchase price of qualified property (such as manufacturing equipment and heavy machinery) as depreciation initially instead of over the life of the asset. This allows the taxpayer to recover the cost of the asset more quickly.

Bonus depreciation was introduced in the 2002 federal Job Creation and Worker Assistance Act,[1] which allowed qualified property to be claimed at 30% if purchased during a certain time period. Subsequent acts have extended and adjusted those time periods and allowed bonus depreciation between 30% and 100%. The federal Tax Cuts and Jobs Act (TCJA)[2] raised the amount eligible for bonus depreciation from 50% to 100% for property acquired and placed in service between September 27, 2017, and January 1, 2023.[3] (Then, beginning in 2023, the percentage will decrease by 20 percentage points per year until it goes to zero in 2027.)

Currently under the act, Michigan's corporate income tax is calculated without accounting for section 168(k) (so the depreciation for that asset is assessed over the life of the asset).

[1] https://www.congress.gov/bill/107th-congress/house-bill/3090
[2] https://www.congress.gov/bill/115th-congress/house-bill/1
[3] https://www.irs.gov/newsroom/tax-law-offers-100-percent-first-year-bonus-depreciation

Section 199 of the Internal Revenue Code, also known as the domestic manufacturing deduction, was repealed December 22, 2017.

The exemption of both sections from the calculation of federal taxable income was intended to offset the revenue that would otherwise be lost due to simultaneous tie-barred changes to the Michigan Business Tax.[4]

MCL 206.607

FISCAL IMPACT:

Based on information provided by the Department of Treasury, if bonus depreciation had been allowable in prior years, revenue would have been reduced by $23.4 million in TY 2017 and $122.2 million in TY 2018. The large increase is due to the provisions of the Tax Cut and Jobs Act, which increased bonus depreciation from 50% to 100% and allowed investments placed into service after September 2017 and before January 2023 to qualify. Because the TY 2018 impact of bonus depreciation reflects more than just one year, it is expected that the impacts in subsequent years will be lower. However, due to taxpayer confidentiality restrictions, it is not possible to generate an independent estimate.

It should be noted that the impact of bonus depreciation is a revenue reduction, as opposed to a revenue loss, in that it does not increase the revenue loss relative to standard depreciation. However, by allowing an investment to be depreciated immediately, the full impact of depreciation is shifted to the state all at once as opposed to being spread out for up to 20 years, depending on the useful life of the asset.

BRIEF DISCUSSION:

Proponents advanced the bill as a way to give immediate relief to business owners who have been hit hard by the COVID pandemic. The ability to claim the full amount of purchased property as depreciation initially instead of over a series of years would allow them to recover the cost quickly and to be able to purchase equipment as necessary to support and even expand their businesses. Although the overall amount claimed would remain the same under current law and the bill, front-loading the benefit would provide flexibility and immediate relief and encourage growth. Some even proposed an amendment to the bill that would make it retroactive to a past date.

However, some responded that those attributes cut both ways: if businesses are able to claim the full deduction up front, that means less paid into the state in taxes for the next few years. Just as businesses have been adversely affected by the pandemic, so, too, has the state. The demands on the state budget remain unchanged, and less revenue recovered from businesses over the next few years (though, again, the overall revenue will ultimately even out) would place even tighter constrictions on an already tight budget.

[4] http://legislature.mi.gov/doc.aspx?2008-SB-1038

POSITIONS:

Representatives of the following entities testified in support of the bill (3-9-21):
- Mackinac Center for Public Policy
- Michigan Chamber of Commerce
- Michigan Manufacturers Association

The following entities indicated support for the bill:
- National Federation of Independent Businesses (3-9-21)
- Grand Rapids Chamber of Commerce (3-9-21)
- Stellantis (3-24-21)

Representatives of the Department of Treasury testified in opposition to the bill. (3-9-21)

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■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.