

APPENDIX B-29: MICHIGAN

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Overview

The Michigan business environment has been suffering in the past few years. Cumbersome taxes have prompted several businesses to flee the state. This exodus is especially evident in the dwindling automobile industry which produces Michigan's signature state product. This economic downturn has produced the nation's highest unemployment rate at 7.5% nearly 3% higher than the national average.¹ The state's signature industry, auto manufacturing, has significantly dwindled within recent years.² In an effort to salvage their state economy and transform their business reputation, state lawmakers and the governor collaborated to replace the Single Business Tax, which was the target of small business owners, with a new Michigan Business Tax in the summer of 2007.³ Time will tell if this change will give the state economy the stimulus that it sorely needs

Forbes, which ranks states on a scale of 1-50 (with a ranking of one being the best), gave Michigan an overall rank of 46 in its 2006 report of "The Best States for Business." This was down another point from the previous year. Each of the primary rankings is listed in the following chart.

¹ "Michigan Unemployment Rate Inches Up To 7.5 Percent." Associated Press WZZM 13. Grand Rapids. 17 Oct. 2007. <http://www.wzzm13.com>

² Bernie DeGroat. "Michigan's Job-Loss Streak Is The Largest Since The Great Depression." University of Michigan News Service. 16. Nov. 2006. <http://www.ns.umich.edu/htdocs/releases/story.php?id=1069>

³ David Eggert. "Michigan Senate Votes To Repeal Business Tax." Associated Press. Lexis-Nexis Universe. Online. 9. Aug. 2006.

Michigan's <i>Forbes</i> Rankings	
Overall Rank	46
2006 Rank	45
Business Costs Rank	40
Labor Rank	44
Regulatory Environment Rank	3
Economic Climate Rank	50

Public Policy

The “State Competitiveness Report (SCR) 2007”,⁴ a study by the Beacon Hill Institute, ranks a state’s ability to produce high income, and generally a better quality of life for its citizens. The rankings compare all the states and rank them 1-50 (with a ranking of one being the best). In this study, Michigan ranked 41st out of the 50 states.⁵ A large factor behind Michigan’s relatively low overall ranking is the state’s business incubation record, or its effectiveness in creating and growing business within the state. This particular category, which examines businesses of all sizes, placed Michigan’s business incubation ranking in the bottom 10 states. The study was particularly critical of Michigan’s highly unionized workforce (45th) and poor record of creating new jobs (39th). It should also be noted that Michigan has the worst employment rate with nearly 7.5% of the population out of work. Moreover, the fact that the state also holds a low ranking in statewide security and crime prevention (44th), may further contribute to business leaders reluctance to start a business in the state and create jobs.

Michigan’s ranking improves slightly when compared to other states in the region. Other Midwestern states, such as Illinois⁶, have a slightly better overall score at 36th, while Ohio⁷ and Indiana,⁸ which rank 45th and 44th respectively, score below Michigan. Additionally, the Beacon Hill study does find a few noteworthy elements of the state economy to praise such as the state’s openness (economic connection to the rest of the world), where Michigan ranks highly when attracting foreign investment, and sending exports out of the state. Michigan also fared better in a similar study, “The Small Business Survival Index 2007 (SBS)”,⁹ where it placed 6th overall. This study ranks states based on whether their policies are “business-friendly” and praised Michigan’s personal income and corporate income taxes.¹⁰ However this study also criticizes the

⁴ David Tureck, Jonathan Haughton, Frank Conte, Christopher Doyon, State Competitiveness Report 2007. Boston: Beacon Hill Institute for Public Policy Research at Suffolk University, December 2007. 37.

<http://www.beaconhill.org/Compete07/Compete2007State.pdf>.

⁵ Tureck et al.

⁶ Tureck, et al 38,50,29.

⁷ Tureck, 50.

⁸ Tureck, 29.

⁹ Raymond J. Keating, Small Business Survival Index 2007: Ranking the Policy Environment for Entrepreneurship Across the Nation 12th Annual Edition. Small Business & Entrepreneurial Council, Washington, DC, Nov. 2007. 2.

http://sbecouncil.org/Media/pdf/SBSI_2007.pdf?CFID=514256&CFTOKEN=91743709.

¹⁰ Keating, 28-30.

state for high levels of spending per capita over a five year projection. Moreover, the SBS index's favorable treatment of Michigan's tax policies run counter to tax-specific studies and also the frustrations of state business leaders.

Regulatory Affairs

Despite a 30 year history of an obscure tax structure that has harmed job growth in the state; the state's regulatory policies have received a relatively positive ranking from most business surveys.

Forbes ranked Michigan's regulatory environment as the third best in the country.¹¹ The Tax Foundation's 2007 State Business Tax Climate Index (SBTC) reinforces this data by showing moderate rankings for Michigan's Labor Cost with moderate costs for both worker's compensation¹² and unemployment.¹³

However, despite the overall positive rankings, Michigan is still saddled with some of the highest energy costs in the country.¹⁴ The state is ranked among the five worst gas tax rates in the country.¹⁵ Additionally when examining the expense of electric utility rates, Michigan falls in the bottom half of all states.¹⁶

Tax Policy

The Tax Foundation's 2007 SBTC index¹⁷ puts Michigan near the bottom, ranked 49th, in corporate tax climate and 45th in the nation on unemployment insurance tax. By comparison, Indiana and Ohio ranked 10th and 11th respectively on unemployment insurances taxes.¹⁸

In addition to the Tax Foundation report, the Council on State Taxation (COST) rated Michigan slightly above average with an overall "B-" ranking in its "The Best and Worst of State Tax Administration" report.¹⁹ In that document, Michigan was praised for its due date on state returns and policy regarding the independent dispute process. At the same time, the report also levied criticism at the state for not having "even-handed"

¹¹ Kurt Badenhausen. "Special Report: The Best States for Business." *Forbes Magazine*. July 2007. http://www.forbes.com/business/2007/07/10/washington-virginia-utah-biz_cz_kb_0711bizstates.html

¹² Keating, 37.

¹³ Keating, 38.

¹⁴ Keating, 40.

¹⁵ Keating.

¹⁶ Keating, 36.

¹⁷ Chris Atkins and Curtis S. Dubay. *Background Paper: 2008 State Business Tax Climate Index*. October 2007, Number 52. The Tax Foundation. 4. <http://www.taxfoundation.org/files/bp52.pdf>

¹⁸ Atkins and Dubay.

¹⁹ Douglas Lindholm and Stephen Krantz. *Scorecard on Tax Appeals and Procedural Requirements*. Council on State Taxation. April, 2007. http://www.statetax.org/Content/ContentGroups/Home_Page_Content/COST_Studies_Articles_and_Testimony/2007BestAndWorstScorecardAmended.pdf

policies and a shortened protest period. Furthermore, 2006 SBS index ranked Michigan in or near the top third of states for its personal income and capital gains tax rates.

While Michigan has received a mix of positive and negative reports in these studies, public sentiment from local business leaders reflected frustration with state tax policies that were poisoning the business climate. In an effort to combat this, the governor and the state legislature took a major step forward to improve the state business climate by replacing the long-standing and cumbersome Single Business Tax (SBT) with the new Michigan Business Tax.²⁰

The SBT was created in 1976 as a method to consolidate several different taxes related to business.²¹ The tax specifically took revenue by targeting the value of services obtained by a business making more than \$350,000, thereby creating a “Value Added Tax” (VAT).²² The areas that were liable for taxation included: labor (or payrolls), capital, and profit to form the base of the tax. Under the traditional terms, any businesses making more than the \$350,000 limit in gross receipts would be liable under the tax.²³ This tax was routinely criticized for harming small business by forcing small business owners to pay a tax on their payroll and creating a disincentive for business owners to hire more people, thereby contributing to the highest unemployment rate in the nation.²⁴

Following a popular election to repeal the SBT in 2006, state legislators created the new Michigan Business Tax (MBT) which was created as a viable substitute to resurrect the state business climate without losing any state revenue.²⁵ The new tax works in much the same way as the SBT by creating a value added tax on capital and profit determined from the companies’ gross receipts. However, the tax on payroll was eliminated in an effort to get small business leaders to begin to hire more people.²⁶ This new structure is expected to deliver tax cuts to seven out of ten Michigan businesses.²⁷ Finally, the tax also includes a revenue limit where anything in excess of the budget plus 5% will be divided with half going back to contributing businesses and the other half being contributed to the state budget stabilization fund.²⁸

²⁰ “Granhom Signs New Business Tax Law.” Associated Press. Lexis-Nexis Universe. Online. 12 Jul. 2007.

²¹ “The Michigan Single Business Tax: Should It Be Replaced Or Reformed?” November, 2003. Michigan League For Human Services. 1. <http://www.milhs.org/Media/EDocs/SingBusTax.pdf>

²² “Single Business.” Outline of the Michigan Tax System. Citizens Research Council. 24 Jan. 2007. <http://www.crcmich.org/TaxOutlinecombine>

²³ Citizens Research Council.

²⁴ Rich Lowry. “The Sick Man Of The Midwest: Michigan, A Liberal Failure.” National Review Online. 18 Sep. 2006. National Review Online. <http://article.nationalreview.com/?q=NWY5ZmMyNjRhMjEwOWJiMjcyMDE5MTI2MWVhNTgIODc=>

²⁵ David Eggert. “Deal Reached on Business Tax Replacement.” Associated Press. Lexis-Nexis Universe. Online. 18 Jun. 2006.

²⁶ Eggert.

²⁷ “Granhom Signs New Business Tax Law.” Associated Press State and Local Wire Service. Lexis-Nexis Universe. Online. 6 Jul. 2007.

²⁸ “Agreement Reached On Single Business Tax Replacement.” Michigan League for Human Services. 6 Jul. 2007. www.milhs.org/Media/EDocs/SBTReplacementTax_Agreement4.pdf

In an effort to help stabilize the state budget deficit, legislators passed a “Services Tax” in the fall of 2007.²⁹ This tax would extend the state’s 6% sales tax to business services that are “discretionary purchases”. These services include, but are not limited to: consulting, security systems, and warehousing. Soon after the tax was signed into law, several Michiganders began circulating petitions for the repeal of the tax.³⁰

Innovation

To measure innovation in the state, investment and returns in innovative activities such as patents and research and development expenditures were examined. National studies that rank the states for their progress in innovation and technology have been extremely complimentary toward Michigan. The New Economy Index³¹ (NE) rates the states according to advancements in innovation (with a ranking of one being the best). In this index Michigan received an above average overall ranking of 19th in the country. The index was particularly complimentary toward the state’s utilization of e-government which the NE declared to be the best in the nation. Additionally, the index also praised Michigan for a high industry involvement in research and development, ranking the state 4th in this particular category. However, the study was particularly critical of the level of entrepreneurial activity in the state, and ranked it 40th in the country.

The SCR has also placed Michigan above the majority of the states with a technology ranking of 17th. Michigan has been ranked 13th overall in patents per capita.³² However, according to the Michigan Department of Labor and Economic Growth’s report, the state is only slightly ahead of the national average.³³ Furthermore, Michigan’s growth has stagnated in patent production and its current rank is down from its 11th place held in 2000.

Michigan’s patent ranking loses more of its luster when following the growth trends in the 21st Century as compared to the US rate of growth during the same period. From the years 2000 to 2006, the national growth in patents was nearly six times that of the state of Michigan. Furthermore, over the past 12 years US patents grew at a rate of 4.6% while Michigan grew at a rate of only 2.5% during the same period.

Workforce

Michigan receives a below average ranking when it comes to its workforce. The SCR ranks the quality of its workforce in its “Human Resources” category. Michigan ranks

²⁹ David Eggert. “New Tax Confuses Businesses As Start Date Nears.” Associated Press State and Local Wire Service. [Lexis-Nexis Universe](#). Online. 21 Oct. 2007.

³⁰ “Backlash Against Tax Hike May Bring Recalls, Petition Drive.” Associated Press State and Local Wire. [Lexis-Nexis Universe](#). Online. 5 Oct. 2007.

³¹ Robert Atkinson and Daniel K Correa. [The 2007 State New Economy Index.: Benchmarking Economic Transformation in the States.](#) Innovation Technology and Innovation Foundation. February, 2007. 13. http://www.kauffman.org/pdf/2007_State_Index.pdf

³² Tureck, et al. 37.

³³ Mark Reffit and Carol Sorenson. “Innovation Indicators: A Report To The Council For Labor And Economic Growth.” Michigan Department of Labor and Economic Growth: Bureau of Labor Market Information and Strategic Initiatives. August, 2007. 3. http://www.milmi.org/admin/uploadedPublications/1296_Innovation_Indicator_Report_2007.pdf

33rd in the country in this category.³⁴ While the SCR notes that Michigan has a large number of scientists as a part of the workforce, the state receives particularly low ratings for having the worst employment rate in the nation. Additionally, the SCR also gave Michigan a poor ranking (43rd) for the number of adults in the workforce.

Overall, Michigan has a poor reputation on labor issues in *Forbes 2006 report*, "The Best States for Business". A few key points are listed below:

- Michigan currently has the worst unemployment record in the country. The 7.5% unemployment rating outpaces the national average by nearly 3%.³⁵
- The state's signature industry, auto-manufacturing, has lost 336,000 jobs from mid 2000 to 2006 and is projected to lose a further 33,000 in 2007 and 2008.³⁶
- The state has a highly unionized workforce at 21.8 %, much higher than the national average of 13.5%.³⁷ According to the Beacon Hill report, only four states have a higher unionized workforce than Michigan.³⁸

However, given the challenges posed by the state economy, there are a number of positive factors related to the state workforce as well:

- Michigan leads the national average of citizens in the work force with high school degrees and some college experience. However the state does lag slightly below the national average of workers with a bachelor's degree or higher.
- The Beacon Hill Competitiveness Study reports that the state ranks 13th overall with number of workers in the science or engineering industries. Meanwhile the State department of labor study ranked Michigan 9th overall in a study that includes the District of Columbia.³⁹
- The Department of labor study shows that scientists and engineers account for 3.69% of the state workforce.⁴⁰

Education

A recent report by the US Chamber of Commerce, "*Leaders and Laggards: A State by State Report Card of Educational Readiness*",⁴¹ gave the state an overall average education ranking while noting several categories where the state could improve. In particular the state has most of its young students starting at or just below the national

³⁴ Tureck, et al. 22.

³⁵ "Michigan Unemployment Rate Inches Up To 7.5 Percent."

³⁶ DeGroat.

³⁷ "Union Affiliation Of Employment Wage And Salary Workers By State". Union Membership (Annual). United States Department of Labor: Bureau of Labor Statistics. Table 5. 26 Jan. 2007. <http://www.bls.gov/news.release/union2.t05.htm>.

³⁸ Tureck, et al.

³⁹ Reffit 6-7.

⁴⁰ Reffit.

⁴¹ The Institute for a Competitive Workforce. Leaders and Laggards: A State by State Report Card on Educational Effectiveness. US Chamber of Commerce, 2007. <http://www.uschamber.com/icw/reportcard/default>

standards for math and reading. The report also criticized Michigan students' lack of English and science proficiency among older students. These factors may partially explain why Michigan high school students fall just below the national average for high school graduation rates and college enrollment.

The same report says the state is doing a good job in terms of teaching quality and school administration. The report praises the state for requiring teachers to take subject matter examinations before teaching a particular subject.⁴² Furthermore, the report also gives high marks to the state for allowing school principals and local officials to have ample freedom and flexibility to run their own programs.

Finally, the State Department of Labor and Economic Growth's report indicates that the state has 44 four-year colleges.⁴³ This amounts to approximately 4.5 colleges per million people. This statistic places Michigan behind Indiana (6.1 colleges/mill), Ohio (6.0 colleges/mill), and Illinois (5.8 colleges/million).⁴⁴

Cost of Market Entry

The Milken Institute releases an annual study in which it ranks the states with the highest cost of doing business on a scale of 1-50 (with a ranking of 50 being best for business).⁴⁵ In this study, Michigan was given a relatively mediocre rating with the 20th highest cost of doing business.

The costs of utilities in Michigan are some of the highest in the country. With regard to the gas tax, only four states (California, Connecticut, Illinois, and New York) had a higher tax.⁴⁶ Additionally Michigan's electricity tax ranks 32nd among all the states and the District of Columbia.⁴⁷

Michigan's combination of complicated tax structure and high unionization rates has prompted several businesses to flee the state. Even the state, which is closely identified as one of the chief driving forces of the Michigan economy, is losing thousands of jobs a year.⁴⁸ As a result, Michigan currently has the nation's worst unemployment rate.⁴⁹ Although the value-added Michigan Business Tax (MBT) is seen as a great tax compromise that will resurrect the state business climate, the state legislature is still passing taxes such as the Services Tax of 2007 on discretionary business practices which have sparked the ire of many business leaders.⁵⁰

⁴² The Institute for a Competitive Workforce.

⁴³ Reffit, 5.

⁴⁴ Reffit.

⁴⁵ "2007 Cost of Doing Business Index." Milken Institute. December, 2006.

<http://www.milkeninstitute.org/pdf/2007CostofDoingBusiness.pdf>

⁴⁶ Keating, 40,36.

⁴⁷ Keating, 36.

⁴⁸ DeGroat.

⁴⁹ DeGroat.

⁵⁰ "Backlash Against Tax Hike May Bring Recalls, Petition Drive."