Testimony on the Michigan Jobs and Investment Act Before the House Taxation and Senate Finance Committees

June 1, 2005

Ford Motor Company
Tim Timmerman, Director of State & Local Taxes
Jerry Brown, Director of Michigan State & Local Government

Ford in Michigan

- Ford's Michigan operations:
  - 70 total locations;
  - 14 manufacturing facilities;
  - World headquarters for Ford and Ford Credit;
  - Various engineering and product development locations;
  - Test tracks and proving grounds; and
  - The Scientific Research Lab, Ford's primary R&D center.
- Ford employs nearly 66,000 people in Michigan.
- Ford has invested approximately $9B in capital spending at its Michigan facilities from 2000 to 2004.
- Ford's research and development expenditures in Michigan amounted to approximately $20B from 2000 to 2004.
- Ford's Michigan annual compensation exceeds $6B.
- Ford purchases nearly $22B annually from Michigan suppliers.
- Ford's highest tax bill is in Michigan and its second highest bill is in Ohio.
  - On a comparative basis, we pay 4.5 times more tax on average in Michigan than in Ohio.

Manufacturing in Michigan

- Manufacturing drives Michigan's economy.
- Manufacturers provide over 700,000 jobs in Michigan.
- There are nearly 16,000 manufacturing firms in Michigan.
- Michigan is the auto industry's largest state in terms of facilities and employees.
- Manufacturing:
  - Is responsible for nearly 30% of the compensation of employees in the state. ($37.8B)
  - Comprises 23% of the Gross State Product. ($74B)
    - This far outranks all other sectors. (FIRE -$50.3B, retail - $31.4B, construction - $16B)
- The auto industry:
  - Is responsible for 13.8% of the compensation of employees in the state.
  - Comprises 11.3% of the GSP.
- Estimates by the Council of Michigan Foundations indicate that Michigan's manufacturers set aside more than $1B toward educational, cultural, human services, and other charitable initiatives.

SOURCE: MMA, 2005 Michigan Manufacturing Agenda.

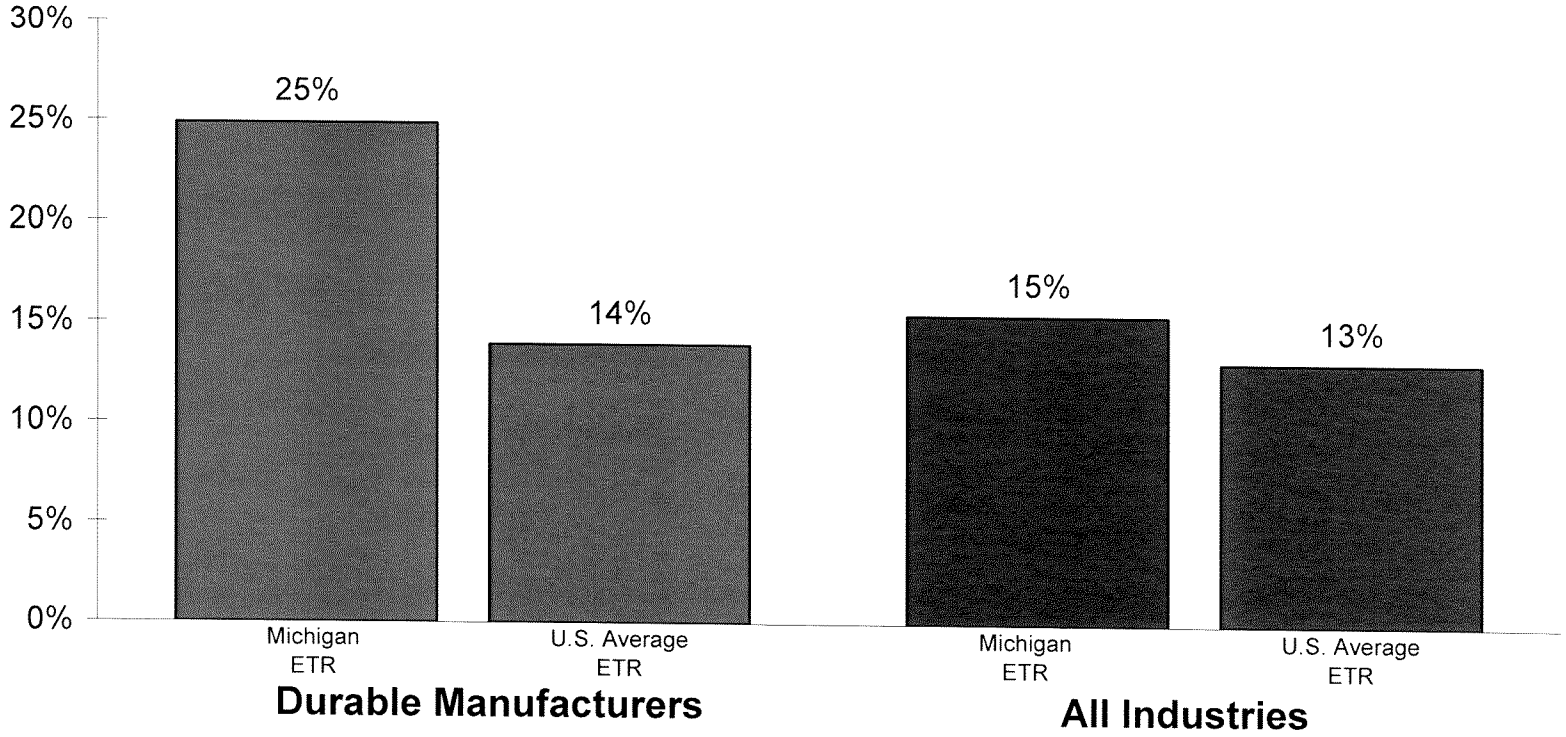
Why Support Manufacturing?

- **Manufacturing's economic multiplier is 2.43 - stronger than any other sector.**
  - Every $1 of a manufacturing product sold to a final user generates an additional $1.43 of economic output, more than half in sectors outside manufacturing.
    - Notably, it is far greater than that of the service sector, which generates only 71 cents of economic activity for $1 of final sales.

  Source: NAM, Published Data from the U.S. Department of Commerce.
- **The manufacturing jobs multiplier is higher than other sectors.**
- **When manufacturers look at Michigan's tax structure, this is what they see:**
  - A system that picks winners and losers;
  - That .7% of the firms pay roughly 50% of the SBT liability;
  - That roughly 60% of businesses don't pay the SBT (147,000/251,000 in 2001);
  - That, in 2006, manufacturers will pay SBT at the highest overall rate; (SBT liability/MI business income)
    - 12% rate for all businesses. ($2,094M / $17,228M)
    - 120% rate for all manufacturers. ($645M / $538M)
  - That, in 2006, manufacturers will pay 43% ($775M / $1,793M) of all personal property taxes.

  Source: Anderson Economic Group, The Tax Burdens of Michigan's Single Business Tax and the Michigan Department of Treasury.

How Michigan Taxes Manufacturers Relative to Other States



- Durable goods manufacturers have the highest effective tax rate in Michigan of any industry (25%) and a rate that is two thirds higher than the industry average (15%).
- This disparity is caused by a combination of high personal property taxes (which many industries don't pay) and a high SBT burden (resulting from the fact that the SBT is largely a tax on capital and labor).
- On average, other states tax manufacturers at a rate that is similar to the taxes paid by other industries. The U.S. average effective tax rate for durable goods manufacturers is 14%, which is close to the U.S. average rate of 13% for all industries.
- Many people have said in their testimony that Michigan is a high tax state. The truth is that Michigan is a high tax state for manufacturers.

Source: Effective tax rates for 2004 calculated by Ernst & Young, Quantitative Economics and Statistics Practice.

Michigan's Heavy Tax Burden on Capital

- Not only are Michigan taxes on manufacturers high, but they directly target the engine of economic growth – capital investment.
- A recent Ernst and Young study on business tax burdens by state indicates that for FY 2003, Michigan's business taxes as a percentage of capital income were the 6th highest in the nation.

  Source: Ernst & Young, A 50 State Study of the Taxes Paid by Business in 2003.
- For the period 1998-2003, Michigan's economic growth rate was 47th among 50 states and 31% below the U.S. average.

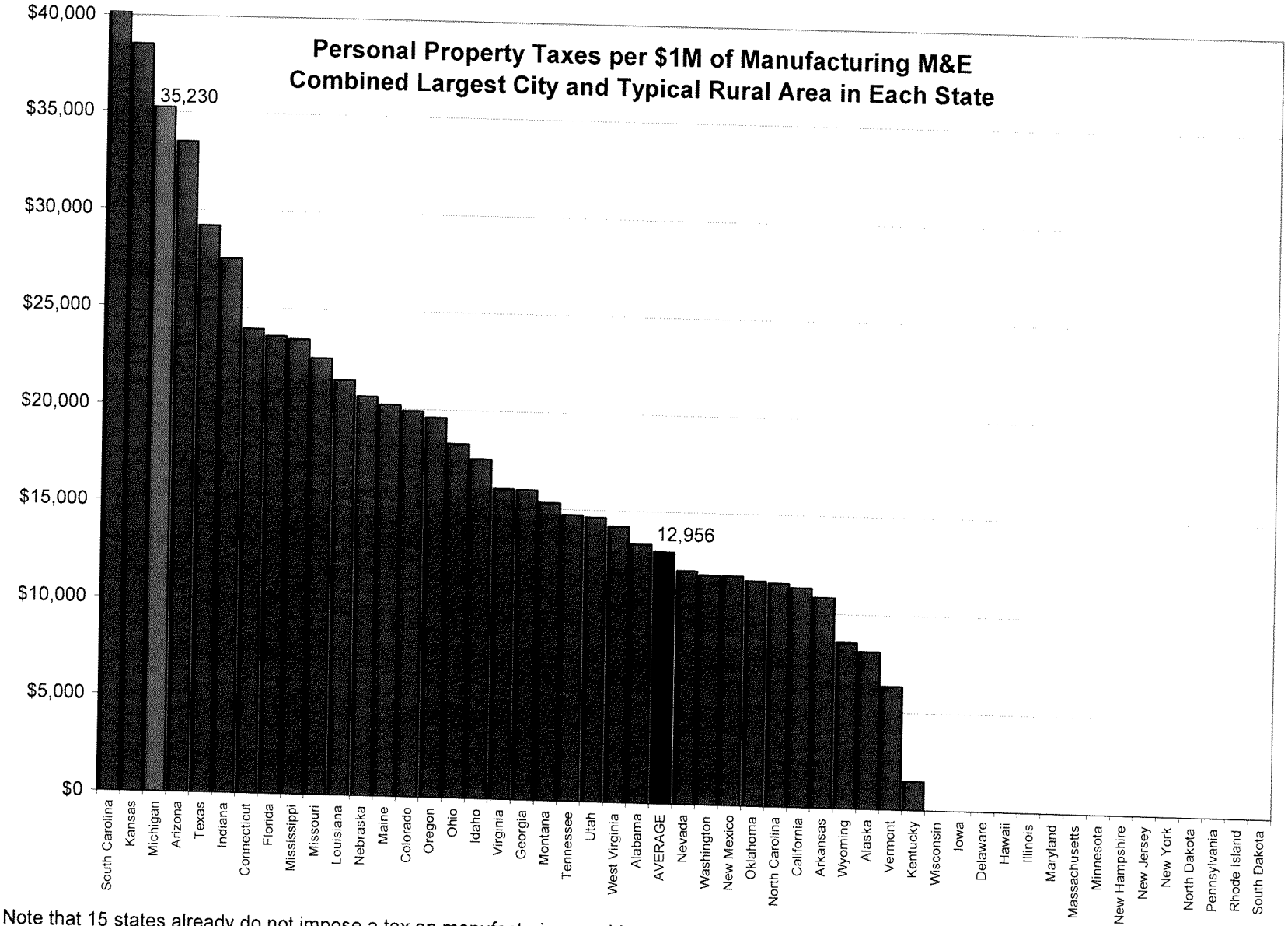
  Source: U.S. Bureau of Economic Analysis, Comprehensive Revisions of Gross State Product. January 2005.
- There appears to be a strong correlation between the taxation of capital and economic growth.
  - For example, fourteen out of fifteen states that did not tax manufacturing equipment had higher growth in state gross product, the broadest measure of a state's economy, than Michigan from 1998 through 2003.
- Reducing Michigan's tax burden on capital may be the most effective way for Michigan to improve its economic growth.
- Manufacturers decide every year where to make capital investment.
- This capital investment is extremely mobile and Michigan is currently at a competitive disadvantage in attracting this investment.

Michigan's Current Tax Structure is a Barrier to Economic Development

- The Governor's proposal addresses three significant barriers to economic development in Michigan.
- The taxation of compensation and depreciation is a penalty on new Michigan jobs and investment.
  - The proposed SBT rate cut reduces this penalty by 37%.
- Investment in Michigan property and payroll increases the SBT apportionment factor, further increasing the tax.
  - The move to a 100% weighted sales factor completely eliminates this tax penalty.
- Taxation of business personal property in Michigan is an additional tax penalty on new Michigan investment.
  - A credit for personal property taxes paid reduces this penalty by 35%.

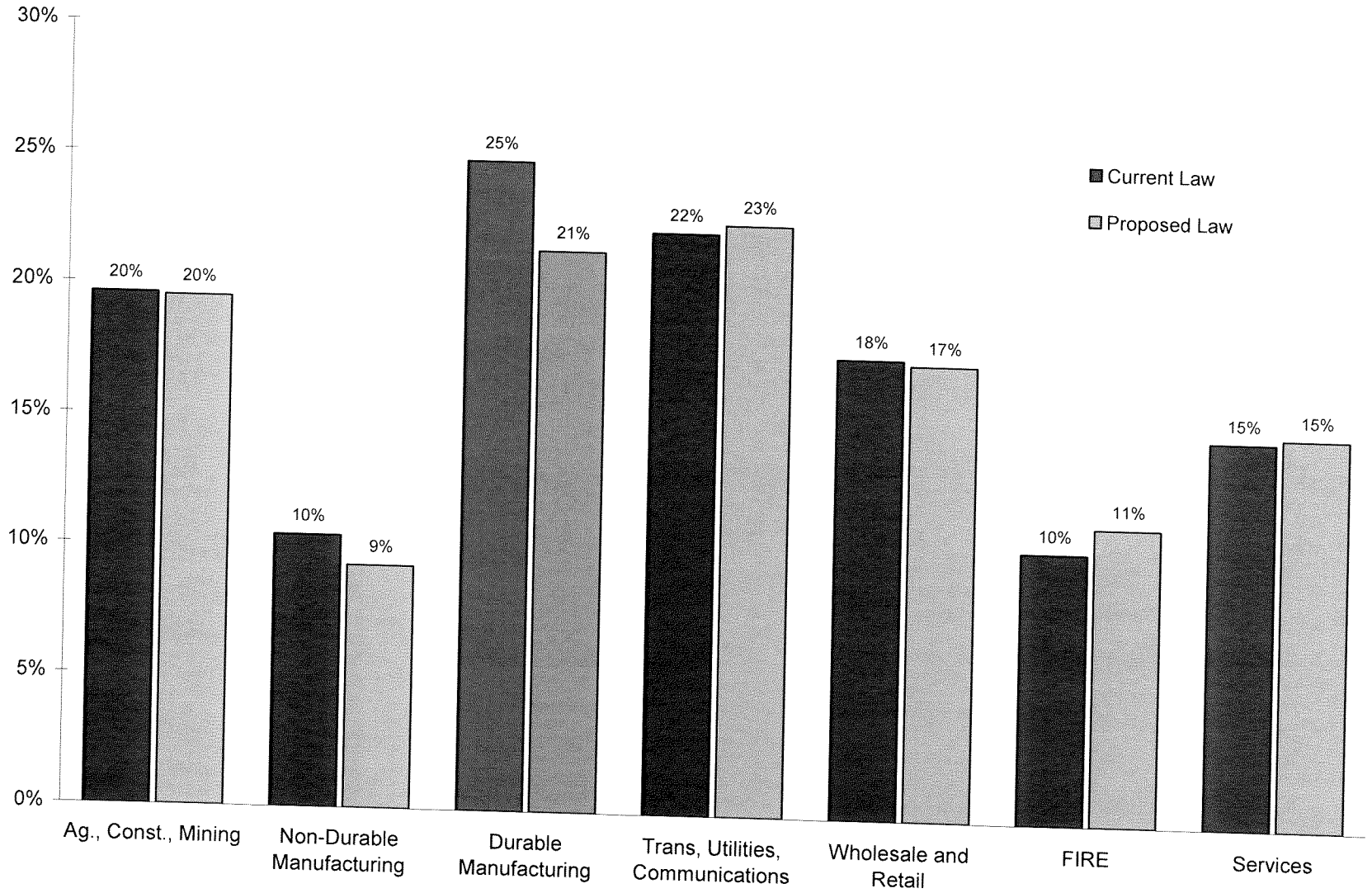
Why Not an Across the Board Tax Cut?

- Still doesn't correct the current inequities in the system.
- You could eliminate the SBT entirely and durable goods manufacturers would still be paying Michigan taxes at higher than the national average for all industries. (18% vs. 13%)
- The real problem is Michigan's heavy tax burden on capital investment.
  - Michigan's personal property taxes are the 3rd highest in the nation.



Note that 15 states already do not impose a tax on manufacturing machinery and equipment.
In addition, the six highest states really drive the average upwards - the average would be $10,006 if the top six states were excluded.
Source: Analysis of Minnesota Center for Public Finance Research, 50 State Property Tax Comparison Study, March 2005.

Michigan Effective Total State and Local Tax Rates on Property Income



Source: Effective tax rates for 2004 calculated by Ernst & Young, Quantitative Economics and Statistics Practice.

Summary

- Manufacturing is the largest contributor to Michigan's economy and wealth, especially since many of its products are exported.
- Michigan must do something to reduce its tax burden on capital investment or its manufacturing base will continue to decline.
- Ford supports the MJIA and encourages the Legislature to act quickly to address these serious problems.