

Interest Expense Limitation (IRC § 163(j)): Senate Bill 1097 proposes to decouple from the interest expense deduction limitation in IRC § 163(j). **Support** Michigan’s decoupling from IRC § 163(j).

Michigan should decouple from the interest expense deduction limitation of IRC § 163(j). Many other states have decoupled from IRC § 163(j), including Wisconsin, Indiana, Connecticut, Tennessee, South Carolina, and Georgia. If Michigan continues to conform to the interest expense deduction limitation in IRC § 163(j) it would significantly increase the cost of borrowing money and of doing business in Michigan and could encourage businesses to move to states with more favorable tax laws.

Furthermore, the interest expense deduction limitation provides no material benefit to the state because Michigan already has provisions in place to address improper interest deductions, such as the potential application of transfer pricing principles. The interest expense limitation has also been added at the federal level as a companion to the expensing provisions; the interest expense limitations ensure that taxpayers do not get a double benefit by purchasing certain assets that are eligible for expensing by means of excessive borrowings that would result in an interest expense deduction. Therefore, because Michigan decouples from the federal expensing provisions, it is both logical and fair to decouple from the interest expense limitation.

In addition, conformity with IRC § 163(j) may also require additional resources to respond to the increased complexity caused by having to apply the federal interest expense deduction limitations of 163(j) in Michigan. For example, because Michigan requires combined reporting by groups that may not be the same as the federal consolidated group, separate 163(j) computations would be needed for many taxpayers at the state level. Furthermore, the Michigan Legislature or Department of Treasury would need to spend a significant amount of time drafting rules concerning a myriad of issues, including: whether carried-forward interest expense will be based on the taxpayer’s apportionment in the year that the interest expense is paid or in the year that the interest expense is used; and how to account for the carried-forward interest expense when there is a change of ownership in the taxpayer. This can all be avoided by decoupling from IRC § 163(j).