



Olds Plaza Building, 10th Floor
Lansing, Michigan 48909
Phone: 517/373-6466

TELECOMMUNICATIONS: UNCOLLECTIBLE AMOUNTS

House Bill 4509 with committee amendment First Analysis (3-20-97)

Sponsor: Rep. Barbara Dobb
Committee: Tax Policy

THE APPARENT PROBLEM:

Local and long-distance intrastate telephone services and interstate telephone services, as well as certain similar communications, are taxed under the Use Tax Act. According to testimony from industry representatives, telephone companies for 26 years deducted from their taxes amounts owed by delinquent customers. Although the General Sales Tax Act contains a "bad debt" deduction that permits such conduct, the Use Tax Act does not. After a recent audit of Ameritech, the Department of Treasury disallowed the deduction for uncollectibles. Subsequently, the Michigan Tax Tribunal disagreed with the department's position, and the matter has been appealed to the state court of appeals. Observers say that subsequent related court decisions have cast doubt about whether the tribunal's view will be upheld in this matter. Legislation has been introduced to place in the Use Tax Act a deduction for bad debts or uncollectible amounts owed by customers similar to that in the General Sales Tax Act.

THE CONTENT OF THE BILL:

Local and long-distance intrastate telephone services and interstate telephone services, as well as certain similar communications, are taxed under the Use Tax Act. The bill would amend the act to allow a provider of such services to deduct the amount of an uncollectible account from the calculation of tax liability. The amount would have to be charged off as uncollectible on the books of the service provider. The Department of Treasury could require supporting evidence for any claim of an uncollectible amount.

If the seller provides both taxable and non-taxable services, the deduction could equal the full amount of the uncollectible account only if the account was documented as a taxable transaction. Otherwise, the maximum deduction would be calculated based on the seller's proportion of taxable services to all services. If part or all of an uncollectible account was paid after the seller had claimed a deduction, the seller would have to remit the taxes in the next payment to the department.

The bill would define an "uncollectible account" as any portion of a debt related to the provision of a service for which the price has become worthless or uncollectible in the time period between the date when taxes accrue to the state for the seller's immediately preceding use tax return and the date when taxes accrue to the state for the current return and that is eligible to be claimed or could be eligible to be claimed if the seller kept accounts on an accrual basis as a deduction under Section 166 of the Internal Revenue Code. An uncollectible account would not include any interest on the price, expenses incurred in attempting to collect any account receivable or any portion of the debt recovered, or any account receivable that has been sold to a third party.

MCL 205.98

FISCAL IMPLICATIONS:

The House Fiscal Agency points out that most telecommunication providers have not been paying use tax on uncollectible portion of accounts. Taxpayers currently paying the tax pay about \$1.3 million per year. If all firms were required to pay the tax (on uncollectibles), about \$3 to \$3.5 million would be collected. (Fiscal Note dated 3-18-97)

ARGUMENTS:

For:

The bill would provide a deduction for uncollectible accounts in the Use Tax Act similar to that already found in the General Sales Tax Act. Proponents of the bill point out that if a customer fails to pay a gas or electric bill, the utility can take a bad debt deduction when remitting its sales tax collections. If the same customer fails to pay his or her telephone bill, the company would still be obliged to submit the use taxes on the account if the law does not permit the deduction codified in this bill. Is this fair? Telephone company officials say that companies have taken this deduction for over a quarter of a century, and now the legality of

that practice is in dispute. The bill would settle this issue.

Against:

Why should the state bear the burden when a telephone company customer doesn't pay his or her bill? The use tax is levied on the "use or consumption" of telephone services. When such services have been used or consumed, the tax should be paid. Such a provision reduces a company's incentive to collect delinquent accounts. The bill also could lead to similar claims by other kinds of companies for special treatment of bad debts under other circumstances not currently covered by tax statutes.

POSITIONS:

Among those who indicated their support for the bill before the House Tax Policy Committee were the Telephone Association of Michigan, AT&T, MCI, GTE, and Ameritech. (3-19-97)

The Department of Treasury has indicated its opposition to the bill. (3-19-97)

Analyst: C. Couch
