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NO PREPAYMENT: SALES, USE TAX

House Bill 4942 as enrolled
Public Act 265 of 1998
Sponsor: Rep. Penny Crissman

House Bill 5313 as enrolled
Public Act 266 of 1998
Sponsor: Rep. Kirk A. Profit

Senate Bill 1158 as enrolled
Public Act 267 of 1998
Sponsor: Sen. Glenn D. Steil

House Committee: Tax Policy
Senate Committee: Finance

Second Analysis (7-29-98)

THE APPARENT PROBLEM:

As part of a budget deficit reduction package in 1993, businesses collecting large amounts of sales and use taxes were required to begin pre-paying those taxes. Prior to the acts, companies were required to remit taxes on or before the 15th day of the month for taxes imposed in the previous month. (This means taxes collected in January were due February 15.) Public Acts 17 and 18 of 1993 required large taxpayers to remit taxes by the 18th of the month based on 95 percent of the previous year's tax liability for the same month. (Thus, taxes paid on January 18 are for the whole month of January and are calculated based on the company's tax liability in the previous January or, alternatively, on an estimate of the current month's liability. Each month's payment also involves a "reconciliation" of the previous month's accounts; that is, a reconciliation of the amount paid in the previous month with the actual tax liability.) Currently, this requirement applies to taxpayers (e.g., retailers and other businesses) with a combined annual sales and use tax liability of $720,000 or more. This means the pre-payment requirement applies to businesses remitting at least $60,000 in taxes per month, which translates into $1 million per month in sales.

This measure was designed to improve the state's cash flow at a time when revenues were extremely tight. The accelerated payments have reduced the borrowing needs of the state government by about $5 million or $6 million per year. At the same time, however, the costs of the taxpayers have increased. In fact, because businesses pay higher interest rates than the state, business pay nearly $12 million in additional borrowing and capital costs, according to a study commissioned by the Michigan Retailers Association. There are also administrative costs involved in pre-funding tax payments, bringing the total cost to the private sector to $12.6 million, according to the study by the Anderson Economic Group. Circumstances have changed. The economy in recent years has generated healthy tax revenues, and the state's businesses believe the pre-payment of sales and use taxes can no longer be justified.

THE CONTENT OF THE BILLS:

The bills would alter the provisions that require the prepayment of sales and use taxes by certain retailers to alter the payment schedule, beginning January 1, 1999. House Bill 4942 would amend the General

Sales Tax Act (MCL 205.56). House Bill 5313 would amend the Use Tax Act (MCL 205.94f and 205.96). Senate Bill 1158 would amend the General Sales Tax Act to alter the sales tax collection allowance for businesses. The same provisions for use tax collections is contained in House Bill 5313.

House Bills 4942 and 5313 would require that businesses remit on or before the 15th of the month an amount equal to 50 percent of the taxpayer's liability for the same month in the immediately preceding calendar year or 50 percent of the actual liability for the month being reported, whichever was less, plus a reconciliation payment. The reconciliation payment would be equal to the difference between the tax liability determined for the immediately preceding remittance minus the amount of tax previously paid for that month. A business would have to remit by the last day of the month the lesser of an amount equal to 50 percent of the taxpayer's liability for the same month in the immediately preceding calendar year or 50 percent of the actual liability for the month being reported.

Currently, businesses subject to the pre-payment requirement get a collection allowance of three-quarters of one percent of the tax due from the first four cents of the tax (up to $20,000) if the tax is remitted on or before the 11th of the month and one-half of one percent of the first four cents (up to $15,000) if the tax is remitted after the 11th day and on or before the 18th of the month. Senate Bill 1158 and House Bill 4942 would make the collection allowance one-half of one percent of the tax due from the first four cents of the tax (with no cap).

FISCAL IMPLICATIONS:

The Senate Fiscal Agency reports, based on information from the Department of Treasury, that the bills would produce a net loss in sales and use tax annually of $1.7 million. The reduction in the collection allowance would increase revenues by $1 million and the change in the payment schedule would reduce the state's cash flow and increase the state's need for short-term borrowing, with borrowing costs estimated to increase $2.7 million annually. (SFA analysis dated 6-4-98)

ARGUMENTS:

For:

This legislation represents a compromise between the current requirement that large retailers and other businesses "pre-pay" sales and use taxes to the state and the pre-1993 method of paying taxes collected in one month in the following month. While the legislation no longer requires the pre-payment of taxes, it still requires that taxes be paid in the month collected rather than the month after. The original justification for making larger businesses pre-pay sales and use taxes no longer applies. The measure was enacted to help the state's cash flow when state revenues were lagging. The robust economy of the past few years has produced very healthy revenues for the state. It is time now to lift this unfair burden off the businesses that collect the sales and use taxes. While the pre-payment requirement clearly benefits the state, by reducing its need to borrow, it does this by shifting borrowing costs to the private sector. Moreover, according to industry-sponsored studies, pre-payment of sales and use taxes costs the private sector two dollars for every dollar saved by state government. Taxes now must be sent to the state before they are collected. How can this be justified? Owners of lumber yards, for example, have pointed out that they often extend credit to their customers in construction, which means that payments (and taxes) are not received until 30, 60, or 90 days after the sales transaction. In addition to carrying their customers, which is a competitive necessity, these business owners are required to accelerate their tax payments; this means, in essence, they are extending credit to the state as well. And businesses that cannot borrow enough to pre-pay their taxes face penalties and interest. While this legislation as enacted does not do all that retailers would like, it does lessen the burden somewhat and represents a compromise between the interests of the taxpayers that have been subject to prepayment and state government.

Analyst: C. Couch

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