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SALES TAX EXEMPTIONS: DEF'N OF "IN GOOD FAITH"

House Bill 4891 as enrolled
Public Act 242 of 2000
Second Analysis (7-19-00)

Sponsor: Rep. Clark Bisbee
House Committee: Tax Policy
Senate Committee: Finance

THE APPARENT PROBLEM:

The General Sales Tax Act requires a taxpayer (e.g., a retail seller) to collect the sales tax on transfers of tangible property and remit the tax to the state. Many kinds of transactions are exempt from the sales tax, such as sales to nonprofit organizations, churches, schools, farmers, and industrial processors. When an exemption is claimed, a seller must keep a record of the sale, including the name and address of the buyer, the sale date, the article purchased and the use to be made of it, the sale amount, and the buyer's sales tax license number (if the buyer has a license). If the seller maintains the appropriate records and accepts an exemption certificate from a buyer in good faith on a Department of Treasury-approved form, then the seller is not liable for collections of unpaid taxes if it is later determined that the sale did not qualify for an exemption. Currently, the phrase "in good faith" is defined in the act to mean that the taxpayer "exercised reasonable care and effort to determine that the purchaser was entitled to the exemption being claimed."

Businesses complain that this puts them in the awkward position of having to challenge their customers as to whether goods being sold tax-exempt are being put to appropriate tax-exempt uses. If state tax auditors challenge a tax exempt sale, say business representatives, the company making the sale must go to the customer to determine if the sale should have been tax exempt. The firms argue that the "good faith" standard should be changed so that it could be met simply by accepting from a customer a signed exemption certificate. If state tax auditors then wanted to challenge the sale, the burden of challenging the customers would fall to them and not the company making the sale.

Public Act 254 of 1995 provided for blanket sales tax exemption certificates. A blanket exemption certificate covers all tax-exempt transactions between a taxpayer-

seller and a buyer for a given period of time. This means a separate exemption certificate is not needed for each transaction. A blanket exemption can apply for up to three years, with the period to be agreed upon by the buyer and seller. Businesses have proposed that blanket exemptions apply for up to four years, which they say is also the duration of the sales tax audit cycle and the length of time records must be maintained.

THE CONTENT OF THE BILL:

The bill would amend provisions in the General Sales Tax Act regarding tax exempt sales in the following ways.

- It would provide a new definition for the term "in good faith" in the section of the act that specifies that a taxpayer (e.g., a retailer or other vendor) is not liable for collections of unpaid taxes if the taxpayer maintains the appropriate records and accepts an exemption certificate from a buyer "in good faith". Currently, the act defines "in good faith" to mean that the taxpayer "exercised reasonable care and effort to determine that the purchaser was entitled to the exemption being claimed." The bill would remove that definition and instead define "in good faith" to mean that the taxpayer "received a completed and signed exemption certificate from the buyer." The bill also would replace the current requirement that sellers maintain a record of the use to be made of the article being sold and would instead require a record of the type of exemption claimed.
- It would also allow blanket exemption certificates to apply for up to four years, instead of three years.
- It would require a buyer who is eligible to claim a sales tax exemption or deduction to register on a form prescribed by the Department of Treasury. If a buyer failed to satisfy the requirement six months after notice

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- to register from the department or six months after becoming eligible to claim an exemption or deduction, whichever was later, the buyer would not be entitled to submit an exemption certificate claiming an exemption or deduction until registering. After the department had issued a notice to register, a non-registered buyer would be allowed to claim an exemption in a refund claim filed with the department.

- It would provide to a person liable for sales tax (a seller or retailer) an exemption from the “good faith” requirement for a period to be designated by the Department of Treasury (with the period to be not less than 30 days or more than 60 days and ending before September 1, 2000) if that person submitted to the department copies of all sales tax exemption certificates from buyers claiming a sales tax exemption.

MCL 205.67

FISCAL IMPLICATIONS:

The House Fiscal Agency says, “Since this change would not alter the exemption status of items being purchased, it should not have any effect on state revenues. It is possible that some sales that were previously allowed as tax exempt may now be taxable under the proposed change to the definition of ‘in good faith’, but the revenue impact would likely be insignificant.” (HFA fiscal note dated 2-14-00)

ARGUMENTS:

For:

A business should not be put in the position of harassing and challenging a customer to determine if a tax-exempt sale is appropriate. It should be sufficient that the customer present a legitimate tax exemption certificate. The current “reasonable care and effort” standard is burdensome to businesses. The bill proposes a straightforward, objective definition of “in good faith” rather than a subjective standard. Further enforcement of the sales tax law should be the responsibility of the Department of Treasury. The department should seek out a firm’s customers if it doubts the validity of tax-exempt sales and not require the firm to do it.

Response:

The law has simply required a seller making a tax-exempt sale and accepting an exemption certificate to exercise “reasonable care and effort” in determining if the purchaser is entitled to the exemption being claimed. This does not seem a burdensome requirement. It doesn’t require a company to “harass”

its customers or even “challenge” them. Retailers and sellers are the taxpayers under the General Sales Tax Act; they play an important role in seeing that the act is properly enforced. Without some vigilance on their part, the sales tax could not be administered fairly.

For:

As enacted, the bill contains provisions that reduce the Department of Treasury’s earlier concerns about the administration of the sales tax. Notably, the bill requires all exempt buyers to register with the Department of Treasury. It also provides a mechanism to encourage sellers to provide the department with copies of sales tax exemption certificates from customers to help with the registration program.

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.