

SALES TAX EXEMPTIONS

House Bill 4540 as enrolled
Public Act 102 of 2001
Second Analysis (7-23-01)

Sponsor: Rep. Mike Kowall
House Committee: Regulatory Reform
Senate Committee: Finance (discharged)

THE APPARENT PROBLEM:

Recently, a question has been raised as to whether licensed beer and wine wholesalers, who are restricted under the Michigan Liquor Control Code to engage almost solely in the wholesale sale of beer and wine to licensed retailers, should be subject to the collection of sales tax exemption certificates as required under a provision of the state tax laws. (See *Background Information* for the only exception.)

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. An exemption from sales tax can also be claimed if the sale of the goods is for resale. (When goods are sold for resale, such as when a wholesaler sells to a retailer, it is the retailer's responsibility to collect and remit the sales tax when the item is later sold to a consumer.) 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 type of exemption made (e.g., resale), the sale amount, and the buyer's sales tax license number (if the buyer has a license). In addition, the seller must accept an exemption certificate on a Department of Treasury form from the buyer. If a taxpayer maintains the required records, and accepts an exemption certificate from the buyer in good faith, the taxpayer is not liable for collection of any unpaid tax if it is later found that the sale did not qualify for an exemption.

According to treasury department staff, the requirements for a seller to maintain the appropriate records and to collect exemption certificates for tax-exempt sales is to be applied to all businesses operating within the state. It would appear, however, in light of the regulations imposed on licensed beer and wine wholesalers by the liquor code and the Liquor Control Commission, and because virtually all

of the sales of a wholesaler are tax-exempt, that many beer and wine wholesalers were unaware of the tax code's requirement to collect sales tax exemption certificates from the retailers to whom they sell.

This issue came to light recently when the Department of Treasury conducted a tax audit on a beer and wine wholesaler operating in the southeastern region of the state. Though the wholesaler had the records of his transactions as required under the Liquor Control Code, he was unaware of the requirement under the General Sales Tax Act to collect and maintain certificates of exemption from each of the retailers with whom he did business. According to testimony offered by the Michigan Beer and Wine Wholesalers Association, the wholesaler was given two weeks to obtain the certificates.

However, because the audit covered a three- to four-year period, the wholesaler could not obtain certificates from all the retailers he had sold to because some of the businesses were under different ownership, some of the previous owners had died, and others would not sign the exemption certificate because, like the wholesaler, they had not previously heard that the exemption certificates were required. As a result, the wholesaler had to come to a "compromise" payment for sales tax on sales made to businesses where he couldn't obtain a certificate of exemption, even though by statute it was clear that such a sale would have been tax-exempt.

Since by law wholesalers primarily can only sell to retailers for resale, some feel it is redundant to require them also to collect and maintain certificates of exemption. Legislation has been introduced to exempt licensed beer and wine wholesalers from the requirement to collect exemption certificates for tax-exempt sales.

THE CONTENT OF THE BILL:

House Bill 4540 would amend the General Sales Tax Act to specify that if the record-keeping requirements detailed in Section 17 of the act were otherwise maintained in routine business records, then the “good faith exemption certificate requirement” of the act would not apply to the following:

- A person licensed as a wholesaler by the Michigan Liquor Control Commission who sold alcohol to another person licensed by the commission. The Michigan Liquor Control Code defines a “wholesaler” as a person who sells beer, wine, or mixed spirit drink only to retailers or other licensees, and who sells sacramental wine as provided under the code.
- The Michigan Liquor Control Commission or a person certified as an authorized distribution agent (ADA) for purposes of the sale and distribution of alcohol to a licensed person. Under the Michigan Liquor Control Code, an ADA is a person approved by the commission to store spirits owned by a supplier of spirits or the commission, or to deliver spirits sold by the commission to retail licensees.

MCL 205.67

BACKGROUND INFORMATION:

Exemption certificate: Prior to 1996, a taxpayer had to collect an exemption certificate for each nontaxable transaction. In 1996, Public Act 254 of 1995 took effect. It amended the General Sales Tax Act to provide for a blanket exemption certificate that covers all tax-exempt transfers between a taxpayer and a buyer; therefore, a seller/retailer only has to collect one exemption certificate per buyer for a multi-year period, as opposed to collecting a certificate for each transaction. Public Act 242 of 2000 clarified further that a taxpayer 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”. (For more information, see the House Legislative Analysis Section’s analysis of House Bill 4891 dated 7-19-00.)

Taxable sales by wholesalers: Under Section 607 (4) of the Michigan Liquor Control Code [MCL 436.1607(4)], a licensed beer and wine wholesaler is allowed to sell or deliver beer, wine, and mixed spirit drinks to hospitals, military establishments, governments of federal Indian reservations, and churches requiring sacramental wines. A wholesaler may also sell to his or her own employees to a limit

of two cases of 24 12-ounce units or its equivalent of malt beverage per week, or one case of 12 one-liter units or its equivalent of wine or mixed spirit drink per week. These sales, with the exception of sales of sacramental wine to churches, would be subject to the collection and remittance of sales tax to the Department of Treasury.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill would have no fiscal impact on state or local units of government. (7-23-01)

ARGUMENTS:

For:

The liquor industry is among the most tightly regulated type of business in the state. Licensees must adhere to stringent requirements of the Liquor Control Code as well as Liquor Control Commission rules and orders. By statute, beer and wine wholesalers can only sell to licensed retailers, though there are a few exceptions. Therefore, almost all of a wholesaler’s business is exempt from sales tax.

The statutory prohibition from taxable sales contained in the Liquor Control Code makes beer and wine wholesalers unique among other businesses. Other businesses typically sell products both to customers who must pay sales tax and also to customers who are exempt from paying sales tax (e.g., nonprofit organizations). In addition, some businesses also make both retail and wholesale sales; for such businesses, the exemption certificates clearly document which of their sales are exempt from the collection of sales taxes. However, this is not the case for licensed beer and wine wholesalers. Since almost all of a wholesaler’s business is tax exempt, it is redundant to require a wholesaler to collect the certificates of exemption. The sales tax act should be amended to exclude beer and wine wholesalers from the requirements for collecting certificates of exemption.

Against:

The requirement in the General Sales Tax Act for sellers to collect exemption certificates from their buyers has been the law for many years. More recently, the law was changed to allow sellers to collect a single certificate from each buyer rather than for each transaction in an effort to reduce the burden on those businesses which conduct tax-exempt sales.

However, it is important to regulate businesses uniformly. It is the treasury's practice to use the exemption certificates as the mechanism to determine which transactions a seller is not responsible to collect sales tax on. If a seller can produce an exemption certificate for a particular buyer, then a treasury auditor can easily determine that the seller was not responsible to collect and remit sales taxes on transactions involving that buyer.

In the case of beer and wine wholesalers, a wholesaler need only to collect a signed exemption certificate from each of the licensed retailers with whom the wholesaler does business. Each certificate is good for a four-year period. Then, in case of a treasury audit, the wholesaler need only to produce the certificates to prove that liability for the collection and remittance of sales tax rested on the retailer. This is not an overly burdensome requirement.

Besides, beer and wine wholesalers are allowed to make some sales that require the collection and remittance of sales tax. It might be different if they made only tax-exempt sales. Therefore, they are not unique among businesses, and granting them an exemption from the act opens the door for other businesses to request a similar exemption.

Response:

Wholesalers may make direct (and therefore taxable sales) to their own employees in limited amounts and also to the military, Indian reservations, and hospitals (but only if the sale of wine or beer was to fill a prescription for a patient; otherwise sales to hospitals are tax-exempt). Reportedly, though, such sales represent a minute amount of a wholesaler's business, and the appropriate sales tax is collected and remitted to the state. Though wholesalers are also allowed to sell sacramental wine directly to churches, such sales are also tax exempt. Therefore, practically all of a wholesaler's business involves selling for resale, which is tax exempt. Besides, the information that the General Sales Tax Act requires sellers to maintain is almost identical to the record-keeping requirements contained in the liquor code.

For:

The Liquor Control Commission is the purchaser of spirits for the state and then sells the spirits to licensed retailers. Under a strict interpretation of the law, the General Sales Tax Act could be read as requiring the commission to collect signed exemption certificates from all the retailers (which number in the tens of thousands) who buy spirits from it. It would seem obvious that since the commission does

not engage in retail sales, that all of its transactions with retailers would be tax exempt. It is ridiculous to put such a burden on the commission, at taxpayers' expense, to collect and maintain thousands of exemption certificates when it is clear through statute (the liquor code) that the commission cannot engage in taxable sales of liquor. The bill would exempt the commission from having to collect the certificates. In addition, though authorized distribution agents (ADAs) act only as the warehouse of spirits for the state and do not engage in sales of liquor, the bill would also include an exemption for them so that they would not have to worry about being asked by treasury auditors to produce such certificates.

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