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SFA BILL ANALYSIS

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Senate Bill 509 (Substitute S-3 as reported)
Senate Bill 510 (Substitute S-1 as reported)
Sponsor: Senator George A. McManus, Jr.
Committee: Farming, Agribusiness and Food Systems

Date Completed: 10-8-01

RATIONALE

Farmers and other businesses involved in agriculture often use pallets or other containers to ship or transfer agricultural goods. It has been pointed out that the application of the sales tax to pallets and containers depends upon whether they are purchased or leased. Under the General Sales Tax Act, the sale of tangible personal property is exempt from the tax if the property is purchased for resale. This means, then, that when a farmer purchases returnable shipping containers to move a crop, the containers are tax-exempt if transferred to another entity, such as a processer, and not returned to the farmer. (In effect, the containers have been resold, as part of the sale of the crop.) On the other hand, if the owner of returnable containers leases them to a farmer to move a crop, then the transaction is considered taxable because ownership of the container has not transferred and the "resale" exemption does not apply. It has been pointed out that application of the tax in this manner means that similar containers and pallets, used to ship similar products, are taxable or nontaxable based upon whether the user purchases or leases the containers or pallets. Some people believe that pallets and containers used to ship agricultural products should be tax-exempt in either case.

CONTENT

Senate Bill 509 (S-3) would amend the Use Tax Act and Senate Bill 510 (S-1) would amend the General Sales Tax Act to exempt from the taxes a returnable pallet or container leased to a farmer or other person involved in agricultural production or processing, including a packer, shipper, manufacturer, or retailer.

MCL 205.94 (S.B. 509)
205.54a (S.B. 510)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Currently, a farmer or other entity who needs to ship agricultural products, and who may find it convenient or affordable to rent returnable containers rather than purchase containers, may find doing so to be disadvantageous when faced with a 6% tax liability on the transaction. A person's decision to buy or lease containers should not be influenced by a discrepancy in tax law, particularly when the farmer or entity may have determined that, absent the tax consequences, storage and overhead costs precluded purchasing the containers. The bills would eliminate the need to make such a decision.

Supporting Argument

Current tax law regarding pallets and shipping containers discourages reuse of those materials, which would be environmentally friendly. Returnable pallets and containers transferred on the basis of a lease may be used repeatedly. Pallets and containers sold on a nonreturnable (tax-exempt) basis might be used once and thrown away, absent any incentive for the user to return them to the seller (such as a refundable deposit). By removing the negative tax consequences of leasing pallets and containers, the bills would prevent waste, conserve raw materials, and prevent premature disposal of often sizable, bulky items.

Opposing Argument

While the bills focus on containers used in agricultural production only, the proposed exemptions would extend to property used in shipping. Both the General Sales Tax Act and the Use Tax Act provide exemptions for agricultural production and industrial processing. Exempt from the taxes are sales of tangible personal property used in the tilling, planting, caring for, or harvesting of things in the soil. Further, both Acts exempt property sold to an industrial processor for use or consumption in industrial processing. Neither exemption applies to shipping activities. The exemption for agricultural production ends with harvesting, so shipping after harvest is not part of the exemption (although nonreturnable shipping containers may be eligible for the resale exemption). The industrial processing exemption specifically states in each Act that returnable shipping containers are property not eligible for the exemption. By creating exemptions for leased pallets and containers used in agricultural production, the bills would expand exemptions to an area that has not previously been allowed, and thus would treat one kind of shipping differently than others.

Opposing Argument

The bills would exempt pallets or containers leased to people involved in "agricultural production" or "processing", but neither term would be defined. Also, it is unclear to what degree a person could be "involved in" agricultural production or processing to qualify for an exemption. The bills raise too many questions and would invite future disputes between the Department of Treasury and taxpayers.

Legislative Analyst: G. Towne

FISCAL IMPACT

State Impact: The bills would be expected to reduce State revenues by $91,000 in FY 2001-02. Industry data indicate that the rental and leasing of reusable pallets has exhibited approximately 20% growth per year. Under the data currently available, the proposed exemption would have reduced sales and use tax revenues by approximately $76,000 in FY 1999-2000, and using the 20% growth assumption, the exemption would be expected to reduce sales and use tax revenues by slightly less than $91,000 in FY 2001-02.

Exemptions to sales and use taxes have an impact primarily on revenue sharing and the School Aid Fund. General Fund-General Purpose (GF/GP) funds receive approximately 1.5% of total sales tax revenues. Approximately 66.5% of use tax revenue is GF/GP. Virtually all of the revenue reduction from the proposed exemption would occur with use tax revenues. Consequently, in FY 2001-02, the bills would reduce School Aid Fund revenues by approximately $30,000 and GF/GP revenue by $61,000.

Local Impact: The bills would have minimal impact on local units. Local units would experience an impact only to the extent that sales tax revenues were reduced, as lower sales tax revenues would be available for revenue sharing.

Fiscal Analyst: D. Zin

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